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ROYAL COMMISSION ON TAXATION

Hearing held in Howard Ferguson Auditorium, Sir Daniel Wilson Residence of University College, University of Toronto, Toronto, Ontario, on Friday, the 17th day of May, 1963.

COMMISSION:

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ROYAL COMMISSION ON TAXATION

HEARINGS HELD AT THE CITY OF TORONTO, ONTARIO

May I7, I963

TOPICAL INDEX — VOLUME No. 23

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ANGUS, STONEHOUSE & CO. LTD.
TORONTO, ONTARIO

Toronto, May I7, I963

Anaconda American
Brass Limited.

Volume No. 23

ANGUS. STONEHOUSE & CO. LTD.
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Toronto, May I7, 1963

Mr. & Mrs. E.W. Oddleifson
and Mr. R.S. McConnell — Volume No. 23

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Toronto, Ontario,
Friday,
May 17th, 1963.

/dpw

--- On commencing at 9.30 a.m.

THE CHAIRMAN: Mr. Secretary, it is practically 9.30. I think we might as well start. I doubt if we will have a much larger audience than we have got, despite the notoriety of this particular case. If you would be so kind as to introduce our visitors to us, we will get under-way.

THE SECRETARY: Yes, Mr. Chairman. This morning we have a brief from the Anaconda American Brass Limited. Mr. A.R. McGinn, Secretary and Treasurer of the company, together with his associates, is here. He will introduce his associates and, as well, we have Mr. R.M. Skinner who is representing the firm of Clarkson, Gordon and Company. Mr. Skinner will be speaking to the brief.

I would like to enter this brief into the record as Exhibit No. 68.

--- EXHIBIT NO. 68: Submission of Anaconda American Brass Limited.

SUBMISSION OF ANACONDA AMERICAN BRASS LIMITED

Appearances: Mr. A.R. McGinn
Mr. W.G. Peaker
Mr. G. Laurence
Mr. R.M. Skinner
Mr. J.S. Vanderploeg

THE CHAIRMAN: Good morning, Mr. McGinn, Mr. Skinner, gentlemen. We have read your submission with a great deal of interest. As a matter of fact, it is as good reading as anything which I have had before me. Perhaps that is because the subject is not altogether unfamiliar.

Usually in these matters we like the participants to say whatever they wish to say.

We have prepared a number of questions and to do justice to this important matter, with the care and thought and the interest you put into it, we have asked our Legal Adviser and counsel, Mr. Stewart, to lead the questions. That does not preclude us from asking questions, too, so you will get it on all fronts.

It seemed to me that you were more apt to receive the questions in a logical order, and a professional will, perhaps, phrase them a little better than the amateurs up here.

In all events, we would be very glad to hear anything, Mr. McGinn, that you would care to say before we start our review of your submission.

MR. McGINN: I have no remarks to make. Before we start, I would just like to introduce our people here. Mr. Peaker from our firm. Mr. Laurence from our firm and, as you know, Mr. Skinner from the Clarkson Company.

THE CHAIRMAN: Thank you very much. Don't bother to stand, gentlemen. Most people don't. You have described your company here. I believe we know who you are and the reason why you are here.

Mr. Stewart, will you proceed?

MR. STEWART: Thank you, Mr. Chairman. Gentlemen, I would like, if you have no objection, to start these questions not with the subjects that you expressly dealt with at the beginning of your submission, but with what you say with regard to LIFO, and the first section that I would like to deal with is the section starting on page 16 and

going on to page 28, where you are dealing with the application of the LIFO method to companies such as Anaconda.

My first question would be this: would you consider that there would be general agreement in the accounting profession that the LIFO method is a suitable method for a business or a taxpayer such as Anaconda?

MR. SKINNER: Mr. Stewart, I think so, without doubt. One can never say there is one hundred per cent agreement but no doubt there would be general agreement that this is a suitable method.

MR. STEWART: I am sure, Mr. Skinner, you are familiar with Bulletin No. 5 of the Canadian Institute of Chartered Accountants which was issued in November, 1950, and which deals with the meaning of the term "cost" as used in inventory valuation. You, in fact, quoted from Bulletin No. 5 in this submission.

May I ask if you are in general agreement with what is said in that bulletin?

MR. SKINNER: Yes, we are.

MR. STEWART: You quote, at the bottom of page 17 of your brief, one paragraph from that bulletin, which I don't think I need read, but I observe that the following paragraph reads this way: "If, in calculating the cost of an inventory at any time, a method of cost determination has been used which results in a figure for cost which differs materially from the figure which would result if the then recent cost had been used (as frequently happens when the LIFO method is used) the method followed in determining cost should be disclosed on the financial statements."

Would you agree with that statement?

MR. SKINNER: Yes, we would agree with that. I may say we do, in the company's own balance sheets, we do use the LIFO method.

MR. STEWART: Thinking in this regard, not necessarily of Anaconda, but of companies generally which may be attracted by the LIFO method, do you consider that they are attracted to it basically because they have costs which are appropriately matched against revenues or do they take into account the possibility that this particular method will provide them with some kind of protection or hedge against inflation?

MR. SKINNER: That is a question which is dangerous to answer, using the term "that is generally approached in this way." I have said that there is general agreement that in the particular circumstances of the Anaconda company, in the way it does its business, the LIFO method is appropriate. Some accountants certainly would go beyond that and feel that because of inflation or the possibility of inflation it is desirable to use a LIFO method which prevents showing profit which may not be realized in a cash form so long as the business itself is continuing.

I would say that that view is quite widely accepted in the United States. It has been urged here but not, perhaps, to the same degree. The interest very recently along these lines seems to be more from the standpoint of taxes that are computed in the export markets, the feeling being that perhaps they are bearing a heavier tax burden than some other competitors in other countries and that this method of income determination, if there was

continuing inflation, would have the same advantages for them as for their competitors.

MR. STEWART: I observe, at the bottom of page 19, Mr. Skinner, you put it very succinctly this way. You say: "The LIFO method of inventory accounting results in charging latest cost against sales revenues and, therefore, clearly reflects our method of doing business and results in a proper determination of our income."

Now, I put this to you: may the results of the LIFO method not be that after a period, inventories may be taken into account for this purpose at a figure which is far removed from current replacement costs?

MR. SKINNER: Yes. That is obviously true if the price of the commodities in the inventory have increased substantially over the years.

MR. STEWART: You have been somewhat critical of the decision of the Privy Council in the Anaconda case decided in 1955 and I would like, in that connection, to refer to certain sections of the Reasons for Judgment in that case with which, I am sure, you are familiar, because I would like to get your comments on what they said and I will start with a paragraph which begins towards the end of the judgment. I think it's the fifth last paragraph.

The statement that is made there is this: "Their Lordships do not question that the LIFO method, or some variant of it, may be appropriate for the corporate purposes of a trading company. Businessmen and their accountant advisors must have in mind not only the fiscal year with which alone the Minister is concerned. It may well be prudent for them to carry in their books stock

valued at a figure which represents neither market value nor its actual cost but the lower cost at which similar stock was bought long ago. A hidden reserve is thus created which may be of use in future years. But the Income Tax Act is not in the year 1947 concerned with the years 1948 or 1949: by that time the company may have gone out of existence and its assets been distributed."

Then, in the next paragraph, about halfway through, they say this: "Again, though their Lordships recognize that this appeal must be determined by reference to Canadian law, they notice that in the U.S.A. in a case in which the so-called 'base stock' method was under discussion, Mr. Justice Brandeis used words which are apt to describe the LIFO method. 'In years of rising prices the base stock method causes an understatement of income for it disregards the gains actually realized through liquidation of low-price stock on a high-price market. This method may, like many reserves which businessmen set up in their books for their own purposes, serve to equalize the results of operations during a series of years.'"

Then they refer to the American case in which that statement was made, and they go on: "In this passage the distinction is nicely made between what is permitted for tax purposes and what a prudent businessman may think fit to do."

And then, if I go back to the second paragraph preceding the first one I have read from, in the closing portion of the paragraph I find these three sentences: "An expert witness called for the company observed that he did not imagine any of the company's witnesses would

claim for a minute that there was a quantity of metal then on hand acquired in the year 1936 equal to the quantity which was valued at the then cost. Yet there was no less than six-and-a-half million pounds of copper in the 1947 closing inventory to which the 1936 cost was ascribed. He might have added that year by year the same thing would happen so long as the business went on and existing stocks were not seriously diminished: in 1987 as in 1947 the closing inventory would carry stock to which 1936 costs would be ascribed. This illustrates clearly the LIFO method and shows how far it has travelled from the conception which has prevailed in the assessment of income for tax purposes."

I read those, Mr. Skinner, simply to support my suggestion to you that the Privy Council, rightly or wrongly, was concerned with the fact that under the LIFO method, as they say, the 1936 costs might still be in effect fifty years later in the costing of inventory for tax purposes. The court did not suggest that this was wrong for corporate purposes, but they were concerned whether it was appropriate for tax purposes where you are concerned not with the fortunes of the company over a period of years, but with income which, rightly or wrongly again, is calculated on an annual basis.

I wondered if, perhaps, you could comment on that situation.

MR. SKINNER: I think I might start by reference to the last sentence in the paragraph that you read, which was to the effect, in the Privy Council judgment, that this illustrates clearly the LIFO method and shows how far it

has travelled from the conception which has prevailed in the assessment of income for tax purposes.

One of our fundamental points put before this Commission is that it is not at all clear what the conception of income which has prevailed for tax purposes is.

EMT/ss

In this particular judgment we find the passage not very far from the end in which it is stated in the second place the account of profit and loss to be madeup for the ascertaining of that difference must be framed consistently with the ordinary principles of commercial accounting so far as applicable, and in conformity with the rules of the Income Tax Act, or of that Act as modified by provisions in schedules of the Acts regulating excess profit duty as the case may be.

For example, ordinary principles of commercial accounting require that in the profit and loss account of merchants' or manufacturers' business, the values of the stock in trade at the beginning and at the end of the period covered by the account should be indicated at cost or market price whichever is lower. Although there is nothing about this in the taxing statutes.

In other words, the Privy Council went this far: They say there is nothing in the taxing statutes which says how inventory shall be valued, but the ordinary commercial principles of accounting state that the inventory shall be brought in at cost or market, whichever is lower.

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In this particular case, however, it was our contention that the ordinary commercial principles of accounting held that the cost which was relevant for this company was the cost which was determined under the LIFO method of accounting. It was this that the initial committee of the Privy Council did not agree with. They went part way in saying income should be determined in accordance with commercial accounting principles, and then

having arrived at the phrase "cost or market", they said we then must find out what the actual cost of the actual goods in inventory is. Whatever the state of the law may be on this point, it is our contention that you do not arrive at a consistent and a useful definition of income by taking a phrase and, shall we say, determine it this way, and then take a word and define that word and apply it in a rather mechanical way.

Our contention is that for purposes of income taxation one should look at the result rather than at the specific word in the process of arriving at the result in determination whether the result is a proper definition of income for taxation purposes. We feel that one of the problems with the Canadian Income Tax Act is that it is not clear what we are trying to get at, what income we are trying to tax. It is not defined. We start with an undefined phrase that income is profits. We look to commercial practices, what is profits, but then in particular cases, and far too many of them in our opinion, we depart from business practice in the determination of profits and state this is not satisfactory for taxation purposes. Nowhere is it stated in any ---- to my knowledge nowhere is it stated in any comprehensive way what is income, what is the definition of income which is to govern for taxation purposes, and we think that this is a matter which falls squarely within the boundaries of this Commission's terms of reference.

Our own view on the subject is that the fundamental definition of income subject to tax must conform to the ordinary business definition of income as determined

by recognized accounting methods. We think, however, that you must for purposes of certainty in the Act put in specific rules such as is done with the capital cost allowance regulations, but that these rules should be framed in conformity with the principles which are arrived at in the ordinary commercial accountancy method.

MR. STEWART: I take it it is also part of your argument that the courts can be circumscribed by decisions which were made many years ago, and that whereas I think may be applicable here, a new accounting concept or principle develops because I believe LIFO is a concept of quite recent origin. One could hardly expect the Courts to apply successful cases which were decided at an earlier stage to the new situation which arises through the development of these new principles.

MR. SKINNER: Yes, that would be precisely our view.

MR. STEWART: Well now, I think I should also ask you to comment on some findings which were made by the United Kingdom Royal Commission on the Taxation of Profits and Income in 1955, because they were not subject to the same disadvantage as the Privy Council in that they did not have to take into account earlier judicial decisions.

It seems to me on reading a portion of their report which deals with inventory valuation, that they, too, were concerned about the fact that under LIFO inventories may be taken into account at prices which were established long ago. I think I might refer you in this connection to page 145 of their report and to numbered

paragraph 473 where they say that they do not think that a universal adherence to FIFO should be required, but they go on and I quote:

3 "We think that an adequate control is secured for this purpose if effect is given to the principle that despite rising prices there is no permanent exclusion from taxable income of an element to reflect the fall in the purchasing power of money."

Now, that is the end of the quotation I propose to make from that particular paragraph, but you will remember that the Commissioners went on to set out in Appendix 2 to their report their suggestions as to appropriate methods of valuing stock in trade. That appendix starts at page 477 of their report, and in that appendix, in paragraph 2 they proceed to set out what methods of valuation they recommend. When they deal with cost they suggest that the taxpayer should have a number of alternatives. I think I might mention them.

The first was actual cost of identifiable parcels; the second was FIFO; the third was moving average; the fourth was the standard cost basis and the fifth was what I think we would call the retail method. I observe in passing that they did not include there the LIFO method. Then they have a couple of paragraphs dealing with market and the lowering cost of the market and then they make a suggestion in Clause 4 the first part of which I think I might read:

"Where base or standard quantities of raw materials, work in progress or finished goods

are proved to the satisfaction of the Board of Inland Revenue that the right of appeal on the part of the taxpayer to the Board of Referees to be essential to the proper function of a business, those quantities of the same or similar goods may be valued on the base stock principle adapted so that any net additions to the quantity of stock held are brought into the stock valuation at the average cost of the additions."

Then they go on and deal with the treatment of fluctuations and the size of the inventory, but that I think is essentially the base stock or modified base stock system. Now, those I think are the only methods recommended by that Commission, and again I am bringing this out, because it does seem to me, as I say, that they were concerned about the propriety of the LIFO method, partly at any rate because of the fact that under that method inventory is continued to be taken into account at a cost which was determined many years before the year presently being taken into account for tax purposes, and also I mention it partly because, as I said, that Commission was not circumscribed by earlier court decisions.

In actual fact as you will recall the Anaconda litigation, when this report came out, had just reached the Exchequer Court of Canada stage and was not --- well, if the appeal from the Exchequer Court had actually been argued, the Supreme Court decision had not come out and certainly it had not got to the Privy Council.

I wonder if you would comment further on the

appropriateness of LIFO for tax purposes having regard to what the U.K. Commission said?

MR. SKINNER: First as to your point that the U.K. Commission was concerned about the danger of a permanent exclusion from taxable income, my recollection was that they felt, as they said in this sentence in paragraph 473, that adequate control is secured if effect is given to the principle that despite rising prices there is no exclusion from taxable income of an element to reflect the fall in purchasing power of money. They then went on to say that paragraphs 8, 9, 10 and 11 of the schemes for inventory valuation which they proposed were designed to meet the contingency, to meet this contingency to, and I quote "generally speaking they secure that stock provisions no longer required because of this contingency should be written back to taxable profit".

MR. STEWART: Weren't the contingencies they were concerned with there, or at any rate the ones that they mention, realizations of stock or changes in the nature of stock owing to alterations in traders' business or cessations of business owing to change of ownership?

MR. SKINNER: As I read that, they were concerned and perhaps we have put a different interpretation on it, they were concerned that while income might be properly stated year by year on the LIFO or the base stock method, if ever there was a cessation of business and a realization of the stock, that this should be brought into tax. Of course, this would automatically follow under the LIFO method or the base stock method unless there were

special provisions --- I beg your pardon, this might not also follow, because it might be a gain on realization of a business as a whole. But in any event they recommended safeguards against the possibility of tax being avoided upon ultimate realization, and I think that would be reasonable in any scheme here as well.

C/PB/dpw

I might point out, with the method which was recommended by the Radcliffe Committee, and to which they didn't give the name of LIFO, it was more or less a process of progressive averaging costs of the base stock inventory as it was built up. That method, which is precisely the one we have suggested in Appendix A as being a convenient way to meet the problem that we have talked about under the theoretical term of LIFO.

MR. STEWART: I suppose the results may be somewhat similar, but I suggest to you if the Royal Commission had intended to endorse LIFO it would have been very simple indeed, if they had, to include it in its appendix after it approved the first-in, first-out method.

MR. SKINNER: Well, they just actually - in this recommendation they didn't give the name of the method they proposed. I suppose they would say it wasn't LIFO because it differed in mechanics from the traditional LIFO. They point out it avoids the necessity of identifying any reduction with a particular layer as stock is required under the U.S.A. system. I suppose this is how you get away from the problem that you have old goods in inventory, the problem you have been suggesting we are particularly concerned with. This would be acceptable to this company; in fact, it is what it has recommended as an administrative vehicle for achieving the same goal of reasonable income determination.

MR. STEWART: Well then, do I understand that you are indicating now that you would be happy with the equivalent or substantial equivalent of that?

MR. SKINNER: The method recommended by the Radcliffe Committee, yes.

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MR. STEWART: Would it be the case that the essential difference between the base stock method and the LIFO method is that under base stock your valuation of your basic industry may be reached quite arbitrarily, quite independently of actual cost of that inventory, whereas under the LIFO method your opening inventory is costed on a historical cost basis?

MR. SKINNER: That is right. As I understand it the base stock method might start with completely artificial prices.

THE CHAIRMAN: Mr. Stewart, before you move on to another subject, there is a question I would like to ask with regard to this distinction between the use of LIFO as the best determination of income and as an inflation measure, which I think was what you had in mind a minute ago.

MR. STEWART: Yes, I was getting to that.

THE CHAIRMAN: You carry on.

MR. STEWART: No, please go ahead.

THE CHAIRMAN: It seems to me one must, in approaching this subject, think of it under two heads. Frankly, I had no difficulty with LIFO whatsoever as the best method for determining income under certain circumstances as set by you under the heading "Classical Tests," I think. As I suppose influenced the Radcliffe Commission it became used as a protection against anti-inflationary costs, and of course, the whole base of its use in the States was greatly broadened. It became apparent to all concerned how extremely useful it would be in this connection. What, therefore, concerns me, if one were restricted

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to the classic test very few taxpayers in the country would be able to take advantage of it. Would the rest of the community not have a just complaint when in inflationary circumstances they would not receive the same protection as those who were able to qualify because of the peculiar circumstances of their business or, stated otherwise, wouldn't those who are able to qualify not only receive the benefit of the best accounting as is their due, but they would also receive some protection against inflation whereas others wouldn't; is there any way of avoiding that?

MR. SKINNER: The question is one, really, whether the commodities which are in the inventory of those companies who qualify are commodities which will vary with the general price level and be subject to inflationary trend. It is probably impossible to make any completely positive statement in this regard, but certainly to take the case of the Anaconda company and its principal raw material, copper, the price of this commodity has not affected the general price trend, at least for a matter of the ten years I looked back at, and probably for a few years before that.

There was an increase, certainly, between the period of the depth of the depression and the immediate post-war period in view of the pent-up supply situation at that time. This was, it seemed to me, not so much evidence of general inflationary trend, although it affected all commodities, but rather the peculiar post-war conditions.

One that was observed, the price of copper, although fluctuating widely, has never shown a long-term

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upward trend.

I was just looking last night at the actual result, and I find if we take the ten years, the most recent ten years which are covered in our submission, income determined under the LIFO method would actually have been higher than income determined under the FIFO method. In any particular year there was a tremendous difference. There was one when FIFO income was 50% of the LIFO income and the two following years when the FIFO income was one-third and one-quarter of the LIFO income. Over the whole period, as I say, it was practically on an even keel. The indication is that this, in other words, this particular commodity, with which this company deals, is hardly responsive to the general inflationary trend. It has a price behaviour all its own. I think you might generate that, probably, in thinking of commodities which tend to be quoted, primarily, commodities which tend to be quoted on the world commodity market.

I thought it was interesting when we were looking at the taxation system of other countries to notice, for example, in France that the base stock method was returned there as being particularly adaptable to these listed commodities which are either bought in the world market or local raw materials, the prices of which are closely related to world market fluctuations as listed in Appendix B. You will notice that copper is among them. I don't know if that completely answers your question. This is our view on these particular commodities.

THE CHAIRMAN: It probably goes as far as I can expect you to. I have observed in the Privy Council

5 judgment they speak of 1936 costs remaining in the inventory. If those costs are still there, a figure that is a little over 25 years ago, I would have thought that the change of the value wouldn't have been given effect to if 1936 costs still remain. Well, there may be an answer to that. Perhaps it is an index for change of value or something like that. Perhaps one could say there shouldn't be inflation; that is the Government's responsibility. Thank you.

MR. STEWART: Mr. Skinner, could we get your reaction to this question: is it, in fact, unreasonable, in a period of rising prices, to require a taxpayer to bring into account as a FIFO system does these inventory profits if those profits have not, in fact, been realized, notwithstanding that if prices decline there will be a corresponding loss?

MR. SKINNER: I don't really think they have been realized in any realistic sense. That line of thinking begins on visualizing business as something you can get into and get out of quickly; if the value of your stock increases in monetary terms you can easily realize that and get out of the business and go on and do something else. I don't think that is particularly relevant to modern economy. The majority of business goes in and is in to stay.I don't, therefore, think you can get too far away from the concept of a system of profits taken out of the business.

MR. STEWART: Looking at pages 21 and 22 of your submission you have dealt with the ten-year period ending with 1962 for your particular company. I quite

appreciate that what concerns you about the FIFO method is the fluctuation in profits which occurs as a result of fluctuation in raw material prices, and these fluctuations are set out for the years 1954 to 1958 at the top of page 22. Those are only five of the years of the ten-year period. I observe from page 21 that in the years 1959 to 1962 there is not too tremendous a variation in the spreads as between the LIFO assumption on the one hand and the FIFO assumption on the other. I have been wondering whether we should infer from that that during those four years the price of copper was fairly constant or whether the narrowness of the spreads is to be explained by some other factor.

MR. SKINNER: This is the last four-year period?

MR. STEWART: Yes.

MR. SKINNER: This is explained by the fairly steady price pattern of copper in that period, yes.

MR. STEWART: As a matter of interest, if we are dealing with world prices here or with prices which are a matter of public knowledge, what is the approximate price of copper at the present time? Let me emphasize I don't want the answer to this question if it is not a matter of public knowledge.

MR. SKINNER: Thirty-one and one-half cents per pound Canadian.

MR. STEWART: Again, so that we can indicate the nature of the problem we are concerned with here, the Privy Council decision referred to the price which your company was taking into account for the 1947 taxation year, and referred to the fact that the price of copper in 1936

7 was $7\frac{1}{2}$ cents per pound.

MR. SKINNER: That is right.

MR. STEWART: Well now, I go on to that illustration that you give on pages 24 and 25 of your submission in which you compare the results of LIFO and FIFO on certain assumptions. I observe from that, in this hypothetical case, your opening inventory and your closing inventory would appear to be the same, and that your opening price and your closing price would appear to be the same.

Now, this is a hypothetical question, but I am sure you will have considered it. Suppose, in this illustration of yours, or suppose that, in fact, the prices in the last year with which we are concerned fell below the opening price, I take it that the effect would be that profit computed on the LIFO basis would exceed that computed on the FIFO basis. What do you suggest should take place in such circumstances? Do you consider more particularly that if a person is permitted to use LIFO for tax purposes he must adhere to cost or would you continue the option of lowering cost of market?

MR/ss

MR. SKINNER: In the United States, of course, I believe I am correct in this, they are limited to cost for tax purposes, if they adopt LIFO.

I have never been able to see this in my own thinking on the matter. I have always thought of FIFO and LIFO as being two independent means of arriving at costs each being justified in their own particular circumstances, and that if the lower cost or market option would be applicable to one, it should be applicable to the other.

MR. STEWART: I observe at the end of Appendix C to your submission you do make a suggestion in that regard.

MR. SKINNER: That is right.

MR. STEWART: You suggest that if LIFO costs could be reduced, that if the market subsequently increased, then costs should be taken into the increase as well. The taxpayer would gradually go back to his original cost basis.

MR. SKINNER: That is right. I think that would be necessary.

THE CHAIRMAN: Not necessarily gradually either.

MR. SKINNER: No, probably would go back.

THE CHAIRMAN: If the market recovered the next year the extent it had climbed the year before, it would go back the next year.

MR. STEWART: Quite so. At the bottom of page 27, Mr. Skinner, and at the top of page 28, you refer to submissions to the Department of Finance which were made by a group of lawyers and accountants. Might I ask if the Anaconda Company was represented in that group?

MR. SKINNER: Yes, it was, sir. Rather I should say its solicitors and auditors who act for the Anaconda Company were in that group. The company itself was not.

MR. STEWART: Appendix A, in fact I take it from what you have said earlier from the point of view of the Anaconda Company would be a satisfactory change in the income tax regulations?

MR. SKINNER: Yes, sir.

THE CHAIRMAN: Might I just add one word there: Would that be satisfactory irrespective of the fact it provides for no reduction to market? At least I don't think it provides for a reduction to market.

MR. SKINNER: That is right, it doesn't. I think all I can say it would be less satisfactory, but perhaps something to --- just satisfactory.

MR. STEWART: I am not quite clear whether you are saying that you would prefer that the regulation be provided for reduction to market?

MR. SKINNER: Yes. I think that would be the preference of any taxpayer really.

MR. STEWART: Commencing on page 28, you deal with the proposition the LIFO method might be made available to taxpayers generally and I would ask you there,at the outset, the same question that I asked when we began this morning, namely, in your opinion would there be general agreement in the accounting profession as to the suitability of this extension?

MR. SKINNER: I find it hard to answer that, because I don't know of any poll that has ever been taken. I would think there would certainly be some people who

might disagree.

MR. STEWART: I think that is a fair answer. May I ask you this: Are we to take it that you are in fact recommending the extension to taxpayers generally?

MR. SKINNER: Well, I think the position of this company is that it is not taking that position. It feels this is a matter of almost an economic policy. These are not the fields which it really explored.

THE CHAIRMAN: To make quite sure we all understand the question, Mr. Stewart, when you say generally, you are using it as opposed to the restriction which we normally say is subject to the classical test?

MR. STEWART: That is correct. As I understand this brief, in the section commencing on page 16, and going on to page 28, the Anaconda Company is dealing with the application of LIFO to a relatively small group of which it would be one. Is that correct, Mr. Skinner?

MR. SKINNER: That is correct.

MR. STEWART: Whereas commencing on page 28 the submission goes on to deal with the pros and cons of the extension of the system, or the method to taxpayers generally. That is correct?

MR. SKINNER: Yes.

MR. STEWART: I was struck by one statement, Mr. Skinner, page 30 and it may be that this is just a matter of semantics, but in the last sentence of paragraph 46 you appear to suggest that for certain taxpayers LIFO is the only measure of income. Do you mean that, or do you mean that LIFO is the method which will most fairly reflect that income?

MR. SKINNER: I think that would be a better way of putting it. This is the best measure of income, or it most fairly reflects income.

MR. STEWART: I think that is perhaps quibbling on words. In the following paragraph, paragraph 47, you deal with certain reasons for the general extension of LIFO to taxpayers generally and you suggest, among other things, that LIFO if it were so extended might have a smoothing effect on the economy.

Now, I would like, in that connection, to refer you again to certain extracts from the Radcliffe Report of 1955, and I am going to ask you to comment on these extracts, if you would care to.

I will read, first of all, from page 143, numbered paragraph 468:

> "It would be an incomplete survey that ignored the general economic significance of FIFO in contrast with other methods of computing profits. Its effect is to impose a relatively higher tax charge at a time of rising prices, and a relatively lower charge when prices fall: This is its main importance since stock prices being likely to fall as well as rise over a period, it is not easy to make valid generalizations as to which of the possible methods is the most reliable revenue producer. Associated with rising prices at home..." and I think

they undoubtedly mean domestic..."FIFO has attractions

> in its tendency to repress business activity: With falling prices its attraction is its

opposite tendency. Associated with rising external prices, its economic value must be more debatable, for while it tends to intensify that shortage of liquid funds which was a recent phenomenon, its influence can be beneficial in relieving an exceptional strain on the country's balance of payments."

That is the end of paragraph 468. I think I might also read paragraph 470:

"Our conclusion is that it would not be advantageous for the tax system to contain a requirement that all businesses must use a single prescribed method in valuing their stock in trade for the purpose of computing taxable profits. That makes it irrelevant to consider further the question whether, if there were to be a single method, FIFO would be the most suitable one."

Then I draw your attention to this sentence in particular: "No doubt it..." meaning FIFO "...has solid advantages from the general economic stand-point but the gist of what we have been trying to stress is that businesses are so various in nature that what is the most suitablemethod to reflect the true annual profits of one cannot be expected to be the most suitable method for every other."

Now, I have read those paragraphs, because it seemed to me that in 1955, at any rate, it was considered from an economic point of view that FIFO had certain advantages. Your submission here stresses the possible

economic advantages of LIFO. Now, are these two documents consistent or inconsistent in your opinion?

MR. SKINNER: It seems that there is an inconsistency. One would hardly claim to be a professional economist. As I read the Radcliffe Committee Report it seems to rest on the proposition that if you keep businesses short of cash in a period of rising business activity, this will tend to restrain any excesses in the boom period.

To what extent this is true, I don't know. I would think merely from personal observation that business confidence has a great deal more to do with the decisions in general of improving the economy than the particular cash situation. Undoubtedly it is important.

I might just point out the sentence in the Radcliffe Committee Report following on the one you read which says that: "On the other hand we must characterize as largely theoretical these generalizations about the relevance of taxation policy or accounting technique to the actual course of action of businessmen and a great deal of allowance must be made for the fact that decisions have to be taken long before their tax consequences can be ascertained."

I don't think we can stress as being an earth-shaking conclusion that the use of LIFO generally has a stabilizing effect. I think we would have to state that such conclusions, with any degree of assurance, would require a lot more data and study than we certainly had available to us.

THE CHAIRMAN: Couldn't you make your point,

Mr. Skinner, by stating the best method of determining income surely would produce the best result when the economy is either going down or coming up?

MR. SKINNER: I certainly think that that is a very valid point to make, Mr. Chairman.

MR. STEWART: Mr. Chairman, that concludes the questions which I had contemplated asking on LIFO itself, and if you agree, I might use the limited time remaining to deal with some of the earlier parts of the brief.

THE CHAIRMAN: Before you get off LIFO, I have got one question which I wrote down right at the beginning. I think it is important in this matter. We do know that the use of LIFO would be quite restricted by virtue of the three tests which are generally laid down for LIFO. It is very hard to know just how restrictive this would be. In my own practice as an accountant, I have not seen many cases which required LIFO and which would be able to meet the test.

Mr. Skinner; have you or your clients ever, at any time, tried to take a census of the eligible people for LIFO or could you as an accountant form any opinion as to what the numbers would be?

MR. SKINNER: Well, we attempted in this group which we mentioned here to put forward the proposal some years ago, or we made representations to the Department of Finance to ascertain how many taxpayers might be affected and we had to conclude that it was very difficult to make any statement which was more precise than there did not seem there would be many.

We could think of industries which seemed to be

most probable, such as the non-ferrous and metal processers generally. I had some notes here. Possibly the steel companies. The sugar refinery industry, probably. Possibly, but not certainly the oil refineries. When you got into individual cases, it was very difficult, as you say, to find more than one or two that would appear to be applicable.

THE CHAIRMAN: Yes. It was my own impression that the number would be quite small, but I never devised any means of getting at it, and it may be that the staff of this Commission should do a little work on this and if so, they might address themselves to yourself or your client as being the people in Canada who probably have given more consideration to this matter than anybody else.

If you could be of any help in that way, we would appreciate it.

T/dpw

MR. SKINNER: We would be delighted to be of any help that we can.

THE CHAIRMAN: Is there anything else on LIFO?

COMMISSIONER GRANT: Just one question which I would like to ask. I am looking at the hypothetical illustration of results of using LIFO as shown on Schedule B, profit and loss, shown following page 24. Actually, it is page 25. This is a hypothetical profit and loss set-up, Mr. Skinner. Do the figures used there have any bearing on the proportion or number of times which your inventory is turned over?

MR. SKINNER: Yes, this would be reasonably typical.

COMMISSIONER GRANT: So that your inventory is turned over roughly eight times a year?

MR. SKINNER: No. In our illustration the inventory was around ten million, and the sales varied from thirty-four million to thirty-nine million. These are in pounds. This is a turnover of about between three and four times.

COMMISSIONER GRANT: I am looking at your dollar value.

MR. SKINNER: I think you would get a more precise definition of turnover if you look at volume, physical volumes. Ten million pounds of inventory.

COMMISSIONER GRANT: So that your inventory, then, is turned over on a tonnage or poundage basis. How many times?

MR. SKINNER: Between three and four times. In other words, we have three to four months' supply on hand

2 in raw material and in process, various stages of production.

COMMISSIONER GRANT: So that the relatively narrow turnover of inventory would have a bearing on your leaning towards LIFO?

MR. SKINNER: Yes, but to put it another way, the relatively high investment required in inventory makes it more important for this company to, in effect, hedge its holding by matching sales prices with raw material prices.

COMMISSIONER GRANT: The large inventory which you consider necessary to keep on hand ---

MR. SKINNER: That is correct.

COMMISSIONER GRANT: Has that any bearing in your particular industry to strike situations which, from time to time, do develop outside the country?

MR. SKINNER: I am informed it does not have any particular bearing.

COMMISSIONER GRANT: I am just trying to relate your particular industry to other industries, which might not be confronted with such a situation, but which would be in similar manufacturing as you are.

MR. SKINNER: I would suspect if other industries have a similar cycle of manufacture, they are going to have a similar turnover situation.

COMMISSIONER GRANT: Except that if their raw
2 materials are available to them, say, completely under their own ownership and management and so on, they might not consider it necessary to carry such a large inventory.

MR. SKINNER: I would doubt that, because

3 strikes can occur internally as well as externally if that were the fact that was under consideration.

MR. STEWART: Mr. Skinner, time will permit me to ask only a few general questions on the earlier part of your brief. The first of them is this: you are advocating the elimination of the tax on corporate income, but I am not entirely clear from your brief as to what you think should happen to that income. Are you suggesting that it should escape tax completely? Are you suggesting that it should escape tax until such time as it is distributed to the shareholders? Are you suggesting the income should be imputed to the shareholders as it is earned, or are you carefully staying away from any of those questions?

MR. SKINNER: We are suggesting that the corporation income tax must be largely passed on in prices and in the long run simply on the basis that any individual businessman or group of businessmen, when contemplating an investment in the business project, have an alternative; namely, indirect investment covering bonds or any of the other media of investment. Therefore, they must compare the returns between the two avenues of investment and anything which they receive from a corporation will be taxed in their hands just as bond interest would be.

Therefore, in making the comparison it is the net they can receive after corporation income tax which will be the relevant factor in deciding whether or not to go ahead with the project.

MR. STEWART: May I just interject there? You are referring to an investor. Let us consider the position of the manager of a company. Are you suggesting that when

4 he determines prices for his products he treats the corporation income tax, in effect, as an expense?

MR. SKINNER: I am suggesting that he, as well as the investor, he as the agent, the investor is looking for a return on capital, and the return that is relevant is the return after taxes. You must take this into account when considering a new project. Now, obviously, once he is committed, the laws of supply and demand are going to take over and quite different decisions will apply in the short run.

THE CHAIRMAN: The answer to your question is obviously in the affirmative, but I would have thought Anaconda prices would have been established on the international market rather than domestically, and the change of the Canadian tax rate would therefore not be affected by change in prices, and that it might well be said that in the case of a company trading outside of Canada, or products trading outside of Canada, the prices of them in Canada are determined by international markets and that taxes are more apt to be borne by shareholders. Is that not so?

MR. SKINNER: We are not thinking in terms of just Anaconda's position. This is a generalization.

THE CHAIRMAN: I was asking you primarily, though, with regard to Anaconda, because of that you have more particular knowledge, or I am assuming that, because you are discussing the affairs of Anaconda.

MR. SKINNER: Yes, to the extent that there is this international competition, that would be correct.

THE CHAIRMAN: I raise the question because it

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was discussed previously, and I wished to know whether you were in line with statements made previously.

MR. SKINNER: I do not think we have additional comment on that. Certainly, the Canadian tax is not going to affect the world price - Canadian tax as such. However, we do have taxes in other countries as well, and to some extent there is a similarity of pattern.

MR. STEWART: I am afraid I interrupted you. I think you were going to deal with my earlier question which was, in effect; if we eliminate the corporate income tax, what do you suggest the tax treatment, if any, should be on corporate income?

MR. SKINNER: Yes. I was coming rather the long way round to answer your question.

MR. STEWART: Please go in your own way.

MR. SKINNER: Well, what I was getting at is that it is relevant where the burden of taxation lies in answering that question. If it is correct that the taxation, corporate taxation, is passed on in terms of prices, then presumably, again over a period, prices would adjust themselves to an elimination of corporation income tax. That is, the prices which the businessmen would charge although, of course, you would have to put other taxes on probably to replace that loss of revenue, other forms of taxation.

Therefore, what I am really saying is that the situation is not much different with or without the corporate income tax. You would still have the essential tax which would be borne by the shareholders, the tax on income received by them, and you would still have the question of

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undistributed profits to deal with, but I think you have that question now.

MR. STEWART: Well, I wish we had an opportunity of pursuing that a little further, but I think I would like you, if you do not mind, to go on to another part of your brief. I was not quite clear whether you are suggesting in this brief that in our income tax legislation in this country we should attempt some exact and detailed definition of income.

MR. SKINNER: We are suggesting that the definition of income almost inevitably should run in step with commercial accounting practice, but we go beyond that to say, for reasons of certainty, and for reasons of administrative convenience, it is desirable to have specific sections spelled out which are in conformity with the spirit and intent and philosophy of commercial practice in determination of profits.

Now, this, it seems to me, is just expressing a perfect thing. It is not as difficult a job as it might be made out to be. It does depend on clearing away a lot of the relics of the past both from accounting and from legal precedent.

MR. STEWART: Then, are you suggesting that the principle should be embodied in the legislation specifically that business income be determined for tax purposes in accordance with accepted accounting principles and practices, subject always to express provisions of the Act?

MR. SKINNER: Well, as we have pointed out in here, subject to express provisions of the Act almost tends to become of prime importance.

MR. STEWART: You have just fairly conceded, I think, there would have to be some express provisions dealing with such matters as depreciation.

MR. SKINNER: Yes, but what I am saying; it is more important to make conformity with the best commercial practice, in effect, through those specific sections than it is to put in a section which says it is the intent that it shall be determined in accordance with the best accounting practice, because this would be ineffective unless it is borne out, unless it is supported by a specific section.

MR. STEWART: We had before us some weeks ago, on a preliminary appearance, a Committee of Canadian Institute of Chartered Accountants, and if my recollection is correct the Chairman or a member of the Commission asked that Committee a somewhat similar question and the further question to this effect: if there was a general principle, or general provision, in the Act that except as expressly otherwise provided income should be determined according to accepted accounting principles and practices, accountants would be able to agree on what those principles and practices were.

I think it is probably fair to say that the Committee of Accountants which was present on that occasion found, or some of them found, some difficulty in saying that there would be agreement, but I think they went away stating that they would give that particular proposition some further thought and would deal with it in their subsequent submission to the Commission.

I just give you that by way of background because, as you can see, I am wondering what your answer to the

7 question would be.

MR. SKINNER: Well, my personal view, as I stated, I think there are generally accepted accounting principles.

B/ss

There is a diversity in application to meet specific circumstances, and also for change as conditions are changing. The method of accounting followed in 1900 is quite different from the methods which are being developed to meet more complex business situations today.

MR. STEWART: Isn't it likely there would be differences between income as computed for corporate purposes and income as computed for taxation purposes? I have in mind, for example, the fact our present system of capital cost allowance permits reductions for tax purposes which may not be taken for corporate purposes. There may be expenses which are perfectly proper corporate expenses which may not be treated as reasonable for tax purposes and so on.

MR. SKINNER: Well, I think those are two different things.

MR. STEWART: I am sure they are.

MR. SKINNER: On those specific examples I don't think there should be a difference between an expense which is perfectly legitimate for corporation expense and an expense which is legitimate for taxation purposes. An expense is an expense, and it is a deduction from income, but there may be a difference in the way in which the expense is allowed and for the timing. The tax statute may set rates to make it easy to administer the Act.

MR. STEWART: What you are suggesting may come down to this, that expenses which are legitimate for corporate purposes should also be allowed, if Parliament in its wisdom chooses to permit incentive provisions or otherwise additional expenses be allowed for tax

purposes you would have no objection?

MR. SKINNER: We refer to the matter of incentives here. That gets into the field of policy to which we have some reservations. Our point really is you should arrive at an income figure and then if you wish to go and to give incentives, well that is the prerogative of Parliament. Our view would really be that the provision of incentives in the Income Tax Act is almost riding two horses. You pay a tax on income and you take it away again. This may be the best way of doing it, but ...

MR. STEWART: I quite appreciate that in your brief you put the proposition that tax incentives should be used sparingly and when they are used they should be available to everyone and not to limited groups. As a matter of interest, do you consider our present system of capital cost allowance for tax purposes could properly be classified as incentive legislation?

MR. SKINNER: There are certain aspects of it which contain incentives. By and large, I would say not tremendously. It may have been when it was introduced in 1949. I think the increasing pace of obsolescence in equipment is catching up with the rates which are allowed in the capital cost system. These can vary a great deal from industry to industry and there as an example of what I mentioned that you have one rule which is administratively convenient and providing the shoe doesn't pinch too tightly in any case, it works well.

MR. STEWART: I suppose it is arguable that even this general rule can be discriminatory. I suppose we have what might be described as capital intensive and

labour intensive industries and the capital cost allowance means much more to the first type than it would to the second.

MR. SKINNER: If the capital cost allowance do, in fact, embody an incentive they are discriminatory in that sense, but I really think those responsible for framing the legislation have to look at those problems one by one and they should have always in mind the best accounting practice. There may well be a sort of difficulty as you mentioned between capital cost allowance and depreciation which are arrived at either for reasons of convenience or because it is felt desirable to give an incentive.

MR. STEWART: Mr. Chairman, we are well past the hour and I think ...

THE CHAIRMAN: I think there is one thing on the matter of incentives. I don't want to go by it. I want to take the time and see if I can understand it. I was quite startled by the suggestion that a certain type of incentive reduces itself largely to produce an "incentive on the cheap". It is quite a catchy phrase. I have been always a little concerned myself with the cost to the Government of certain incentives which are given on a really broad base. I suspect that seldom when we see the application of the incentive does it, in fact, result in a change of judgment and only seldom is it what is intended to be accomplished by the incentive. The net is spread very wide and, in fact, sometimes catches only a few. The "incentive on the cheap" is, I think, the kind where the benefit of the incentive will be reaped by those who

actually do what the Government wishes them to do. Ihave in mind primarily one thing which you point your finger at, namely, the addition of 50% of the amount of capital cost expenditures on research. It would seem to me this is a pretty effective kind of incentive.

MR. SKINNER: Quite a lot of money is spent on research.

THE CHAIRMAN: To some extent caused by this incentive. If that is so, it probably is an incentive on the cheap, because tax abatement isn't being cast broadly around catching a few. Is that what you intend by the phrase "on the cheap"?

MR. SKINNER: By the phrase "on the cheap" we mean simply that the taxpayer who set up a research program in 1960 received no abatement because of the way it is written, but the one who sets it up in 1963 does receive anadvantage, and this can only be justified on the basis in the short run there is a real need for some sort of a shot in the arm. It seems to me obvious there is a discrimination between the taxpayer who has paid in 1960 and the one who did it stimulated.

THE CHAIRMAN: I think one must very readily admit there is a discrimination, but would there not always be a discrimination when laws are changed without retroactive effect, sometimes to the detriment and sometimes to the benefit of the taxpayers? Perhaps this is such an aggravated case of discrimination that you are entitled to point your finger at it. I am not sure. That was all I wished to cover there, Mr. Stewart.

COMMISSIONER WALLS: I would like to go back to

page 4, paragraph 7 where apparently you suggest as an alternative to the corporation tax increased sales tax, although you state it would have to be gradually over a period of time. Now, first of all, I presume Anaconda as a firm pays very little sales tax because your product is rarely an end product; am I correct in that?

MR. SKINNER: That would be correct.

COMMISSIONER WALLS: I beg your pardon?

MR. SKINNER: That would be correct.

COMMISSIONER WALLS: What I am interested in knowing, if you are going to attempt to replace the corporation tax predominately with sales tax, do you favour it by doubling the percentage of sales tax or would you rather increase sales tax less and eliminate the exemptions, some of which, I guess, would indirectly affect your business; that is building supplies?

MR. SKINNER: I think we have to answer that we have not gone into this question of how you would replace. We use sales tax as an example. It might be by a completely different method of expenditures or payroll deductions or something else. We haven't attempted to go into that area, realizing it is of interest to you, but also realizing that other people will be speaking to the whole pattern of the tax system.

COMMISSIONER WALLS: I just thought having made the recommendation, perhaps you had given some thought to it.

MR. SKINNER: I am afraid as so many who appear before you we are anti some things, but notso clear on what we favour.

COMMISSIONER WALLS: Thank you. That is all I have.

THE CHAIRMAN: I don't think we have any more questions up here. You are complete, Mr. Stewart?

MR. STEWART: Thank you, Mr. Chairman, yes.

THE CHAIRMAN: Have you anything else you would like to add?

MR. VANDERPLOEG: Mr. Chairman, I was interested
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in Mr. Stewart's remarks in reading from the Radcliffe Report about the effect of FIFO taxation on the rising market and creating more taxation for us on account of unwise business expenditures. In fact it gives the Government more money, which they don't always spend too wisely. The Government are not noted for spending wisely.

Another point he mentioned was that the LIFO was fairly youthful, a fairly callow youth.

THE CHAIRMAN: I am sorry, I didn't hear you?

MR. VANDERPLOEG: He mentioned the LIFO system was a fairly callow youth. It is at least 30 to 40 years old. I daresay there has been more business done in the years since then than was ever done in the years all together before that. For comparison I might mention I read recently that the U.S. budget envisions more spending than all the U.S. budgets previously to the year 1920. While it is youthful in years, it is not youthful in its application in business.

THE CHAIRMAN: Thank you, yes.

MR. STEWART: Mr. Chairman, I might quite agree the life of LIFO appears to be about 30 to 40 years. I

was really raising this point because some of the recent decisions which were referred to by the Privy Council in the Anaconda case went back considerably more than that.

MR. VANDERPLOEG: Things change, of course, and new things have to be resorted to to take care of them. I would like to mention too there was a question if there was a census on LIFO. I believe there was a study by the U.S. Chartered Accountants' Association, or whatever the name is, which approved LIFO, and it was sent, I believe, to a great many American firms in the States. Perhaps our Chairman will recall that.

THE CHAIRMAN: No, I am sorry I don't. I do know that at the time it was introduced in the States that there was a firm belief in that country that its use would be restricted to what we contemplate in Canada, or what you are contemplating in Canada, although that didn't transpire at all. It became much broader. I wasn't aware there was a census.

MR. VANDERPLOEG: I recall that the Crown Counsel, one of the Crown witnesses, Mr. Thompson, I believe, who was opposed to LIFO --- his firm in Canada was opposed to LIFO and his firm in the States was for it.

There is another point I would like to bring up. Maybe this is being a bit vindictive. Appeals to the Privy Council were abolished by Parliament in 1949, September I believe it was, and the then Prime Minister said it was a campaign issue and the country supported it. The Minister of Justice, I think it was Mr. Garson, said appeals to the Privy Council was a touch of colonialism

for Canada and should have been abolished long ago. I think the Prime Minister said it sounds as if our Courts and our lawyers are not smart enough. Then four years later, 1955, the same Government that abolished the appeals took this to the Privy Council. In the intervening years our lawyers and Courts became less smart instead of smarter, you see. To be sure there was a hedge in their abolishing it. They said either party could take it to Privy Council if it was then under consideration by our Courts. Surely that reservation wasn't to be used by the Government.

THE CHAIRMAN: We note your observation. I think we will stop on that point.

MR. VANDERPLOEG: I would like to make these points. Thank you very much.

THE CHAIRMAN: Thank you very much indeed. We are indeed grateful to you gentlemen for bringing this submission to us. We would have been extremely disappointed if you hadn't drawn our attention to LIFO, although I rather suspect somebody else would have. We will certainly give the matter consideration before we report. I don't think it is an easy matter at all. I think we will have to spend a little time with it. We thank you very much, and if as we go forward we need help, we may address ourselves again to you, or to you, Mr. Skinner. In the meantime, many thanks.

We will stand down for five minutes, Mr. Secretary.

---Short recess.

R/dpw

THE CHAIRMAN: Mr. Secretary, would you introduce our visitors to us?

THE SECRETARY: Mr. Chairman, Commissioners, we have before us Mr. and Mrs. E.W. Oddleifson of Bayfield, Ontario, and associated with them is Mr. Stanley McConnell of Toronto, Ontario. These people have prepared a brief which you have received and Mrs. Oddleifson was going to speak to the brief.

I would like to enter it into the record as Exhibit No. 69.

--- EXHIBIT NO. 69: Submission of Mr. and Mrs. E.W. Oddleifson and Mr. R.S. McConnell.

THE CHAIRMAN: Thank you, Mr. Secretary. Good morning, Mrs. Oddleifson and gentlemen. We have read your submission, which we found interesting, and we have a few questions to put to you. Before doing so, if there is anything you would like to say to it, we would be very glad to hear it; to summarize it or speak to it. There is no need to read it.

MRS. ODDLEIFSON: Thank you. Mr. Chairman and Commissioners, I would like to thank you for inviting us here. We are very glad to come. I think we just represent, say, the Canadian individual.

We have no corporation or institution behind us. We have been students of the economic picture for a number of years. Mr. McConnell has written a number of books on the subject and we feel he is the prime mover in getting our submission to you.

I do not think I have anything to add to the brief. Mr. McConnell has a few words he would like to say and we have some additional submissions which will be made, I understand, at the proper time, as well as the brief you already have.

THE CHAIRMAN: Would you tell us what directed your interest to this? Mr. McConnell, you pointed out, is an author of books on economy. Do you teach?

MRS. ODDLEIFSON: No.

MR. McCONNELL: No, I do not teach economics. I approached it from a rather novel point of view. I graduated in engineering from the University of Toronto; that is a way back, and architecture was my particular department.

Shortly after the First World War I became greatly interested in economic problems which were very cruel at that time and from about 1930 on, I think I have devoted practically all my time to studying, research and writing on that subject. That explains my interest.

THE CHAIRMAN: What are some of your books?

MR. McCONNELL: Well, the first one I called "A World on Gold Rations." The next one was "Bitter Fruit," an audit of the capitalistic system.

Then I wrote one called "Now Take Canada" which was in a popular style, conversational style, which I tried to simplify what is, to most people, a rather abstruse subject, and after that, just about the end of the Second World War, I had a book come out called "I Speak for the Centre" which was dealing partly with the ideological problem and the relation of the economics to

that problem.

I have written about twenty different manuscripts that I couldn't get published. The last one published was a little booklet called "And Deliver Us From Inflation" and that one I will be glad to leave several copies here, if it would be of interest to the Commission.

THE CHAIRMAN: Thank you. I would like to read it. Shall we proceed?

MR. McCONNELL: Do you want to shoot some questions at us?

THE CHAIRMAN: That is what I had in mind, unless there is anything else you would like to say to us before we do.

MR. McCONNELL: I had prepared a little summary of our whole brief which I suppose would take about two or three minutes to read.

THE CHAIRMAN: By all means.

MR. McCONNELL: It would, perhaps, give you a picture of what we are driving at. The title of this little brief is "Consumer Taxes: An Economic Deterrent."

We are appearing before the Tax Commission on behalf of the Canadian consumer who is usually inarticulate. Consumer taxes sometimes referred to as indirect or hidden taxes are not a new feature in our economy but dating from the Second World War; they have expanded to the point where they represent over 64% of the total revenue collected by the Government.

I took those figures from the Dominion Bureau of Statistics and worked it out on that basis.

Such taxes include customs and excise duties,

federal and provincial sales taxes and corporation taxes. They are levied at various points in the productive and distributive chains and are usually compounded several times before they are finally paid by the consumer at the retail level. They are much greater than the nominal rates would indicate.

The effect of these taxes is to slow down the economy at a time when the Government is seeking ways and means to stimulate it. A personal income tax merely transfers purchasing power from the private to the public sector and has therefore no appreciable effect on prices. That is to say, if the taxpayer does not spend the money, the Government spends it and so the total expenditures would approximate the same thing. That is, with the direct income tax but consumer taxes do have a secondary effect; namely, raising the price level of all goods on which they are levied, and thus do double the real burden of the tax.

That is our chief contention; that the consumer taxes do double the real burden of the tax and, incidentally, infringe on one of Adam Smith's four principles of taxation. Perhaps I should apologize for bringing Adam Smith into it.

THE CHAIRMAN: Not at all.

MR. McCONNELL: We are leaving copies here of his four principles of taxation. The one to which I am referring now is No. 4: "Every tax ought to be so contrived, as both to take out and keep out of the pockets of the people as little as possible over and above what it brings into the public treasury of the state. A tax may either take out or keep out of the pockets of the people a great

5 deal more than it brings into the public treasury."

Now, consumer taxes are paid once at the wicket, when you buy your groceries, whatever it is, but they automatically raise the whole price level of the country and therefore we believe or claim that is double taxation. It is not efficient taxation.

To continue: Apart from this they are inequitable as they bear most heavily on the lower income groups. They distort the whole system of values and economic rewards in the community, encourage tax evasion and negate the free operation of market incentives under the law of supply and demand. They are, in effect, a statutory markup of the price of goods.

The obvious effect of this is to make Canadian industry less competitive both in domestic and foreign markets, which in turn contributes to our balance of payments problem, which, last year, gave Mr. Diefenbaker a headache. It is a rather serious problem.

As a debtor nation, Canada must soon correct this imbalance or suffer unpleasant consequences. A revision of the tax system to lower production costs would be a long step in this direction.

I was interested to compare the American tax revenue with our own and I found out that in the United States 47% of the national revenue is collected via consumer taxes while in Canada the corresponding figure is 64%, so we evidently rely very much more here on the consumer tax than they do in the States.

In the States about 55% of the national revenue is raised by the direct income tax which, in our brief,

6

we claim to be the equitable system of taxation.

COMMISSIONER WALLS: May I interrupt you? I don't wish to interrupt your statement, but in these figures on the United States you are quoting, are you not, federal sales tax? You are not taking into consideration the amount collected by the States as sales tax?

MR. McCONNELL: No. This refers merely to the federal taxes.

COMMISSIONER WALLS: I think if you had the amount as it is collected by their States you would not get the adverse comparison, perhaps, that you do.

MR. McCONNELL: Well, perhaps not, although all the States have sales taxes - I would not be prepared to say as to that without looking into it further.

COMMISSIONER WALLS: Do these figures include corporation taxes?

MR. McCONNELL: Yes, we include as consumer taxes the corporation taxes.

COMMISSIONER WALLS: I am sorry, go ahead now.

COMMISSIONER BEAUVAIS: In both Canada and the States in your figures?

MR. McCONNELL: Yes.

COMMISSIONER GRANT: I have a table here, Mr. McConnell, which gives the distribution of tax levies at all levels of government which would be the state, national and municipal levels.

MR. McCONNELL: Yes, that should be very useful.

COMMISSIONER GRANT: If you would like, I will read these.

7 MR. McCONNELL: Yes.

COMMISSIONER GRANT: As between Canada and the States. In the United States 65.5% of the taxes came from income tax.

MR. McCONNELL: That is overall?

COMMISSIONER GRANT: Overall. All levels of government. 14.2% capital tax, and 22.3% tax on consumption. Canada: 48.8% income; 17.1% capital - a large measure of that comes from municipal taxes; 34.1% consumption.

MR. McCONNELL: Yes, that more or less bears out my figures in detail. That covers all levels of taxation so, apparently, that would show that in the States they rely more upon direct income tax than we do and less upon consumer taxes. Would that be your interpretation?

THE CHAIRMAN: Yes, we would accept that.

MR. McCONNELL: So, in that respect, at least, I think that they are probably ahead of us. However, to continue: In these times everyone, including the Government, tries to live on inflation, which I would call monetary and price manipulation. We find it a very lean diet. In writing up the price of goods, the Government creates a greater demand for money while lowering the effective demand for wealth. When a recession comes, there is a demand for so-called "easy money." We try to monetize recovery. Interest rates are lowered and the money supply increased by the banking system. This new money is available for loans to business and industry.

The question arises, then, how does this new money get into circulation? Well, the banks, let us say,

8 loan it out to business and industry who want to expand their plant, or for some other productive purposes, but if the consumer demand is lacking, business is not going to expand its facilities. The only way to stimulate the production is to make it easier for the consumer to buy, and that bears directly on the problem of inflation which apparently no one yet has been able to remedy or to stop.

T/dpw

Just to give you a little example of our thinking along those lines, according to the Dominion Bureau of Statistics, they give the gross national product of Canada for the year 1961 as thirty-six billion dollars plus. That is just in round figures, thirty-six billion dollars.

Now, included, to make up that thirty-six billions, there is included an item of some four-and-a-half billion in the form of hidden taxes or consumer taxes. So that is listed as an asset. Another item included in that thirty-six billions, is listed as consumption allowances; now, capital consumption allowances would indicate that that is depreciation of capital, so I claim it has no place in a realistic picture of what our gross national product might be.

If we deduct those two items from the gross national product, we get a figure of something like twenty-seven billions. Now, that is in terms of today's dollar, but if you put it in terms of the 1939 dollar, that big gross national product shrinks to about thirteen billion.

Now, there is a big difference. Where has the money gone? The President of the U.S. Steel Corporation - what is his name?

THE CHAIRMAN: Mr. Blough.

MR. McCONNELL: Yes, Mr. Blough. He referred to their profits as phantom profits because he found out, the company found out, when they wanted to replace equipment that had been installed, say, 20 years ago, they would have to pay two or three times the depreciation that

had been allowed out of profits, so that the profits they thought they had made he designated as phantom profits.

I claim that our figure for gross national product of thirty-six billion dollars, although it might give rise to some complacency and looks good in print, is largely phantom figures. If we were to express it in terms of real wealth, it would, as I have pointed out here, shrink to about thirteen billion in terms of 1939 dollars, because we know that since 1939 the purchasing power of the dollar has shrunk more than 50%.

That is just by way of illustration of how figures - they say figures don't lie, but sometimes they do.

Well, to continue, we point out that consumer taxes are inequitable. They are inequitable because the man of low income spends most of his money in the grocery store at the retail level, so he pays proportionately much higher tax than the man who has considerable means.

Now, this disease of inflation is very subtle and almost incurable, apparently, but as we have pointed out in our brief the Government is partly responsible for it because all taxes levied on goods raise the prices accordingly and lower the purchasing power of our dollar.

So, now, we have these problems confronting us: unemployment, imbalance of international payments, deficit financing, rising taxation at all levels, and a rather sick and lagging economy.

Now, that is the problem with which our new government must deal. If these problems are to be met, policies should be directed to increasing rather than

3 reducing the purchasing power of the dollar. To do that we suggest that sales taxes and consumer taxes should be lightened in favour of the personal income tax. Now, admittedly, that is not considered very expedient. Apparently, human nature being what it is, if you do not see it go out, you do not realize it so you do not react, but the Government imposing added personal income tax might possibly run into quite a bit of opposition.

The first target, I think, should be the sales tax which was a wartime emergency measure that has never been rescinded. Now, if the Government would grasp this nettle firmly, it would set an historical precedent of government vacating a tax field which it had once occupied. There are not many tax fields remaining for governments today outside of the poll tax, but I think the sales tax would be a good place to start to reduce consumer taxes.

It would be a powerful stimulant to the national economy. It would lower all our costs, placing Canadian industry in a better competitive position, and also increasing the buying power of the state's own revenue.

Now, I have not very much more to add, but if we might venture to add a fifth principle to Adam Smith's four principles of taxation, it would be this: the state should tax people rather than goods. Any tax which appears in the price of goods tends to disrupt the vital economic processes by lowering the purchasing power and productivity.

What the state really wants is not more tax money but more national wealth to tax, at lower rates, if possible.

That is a brief summary of our submission, and

4 if there are any questions we will be very glad to answer them.

MR. ODDLEIFSON: Could we include, Mr. Chairman, the copies of this particular brief as an exhibit?

THE CHAIRMAN: By all means.

MR. ODDLEIFSON: Or it is an addendum, rather. Also, we do have listed the four principles of Adam Smith.

THE CHAIRMAN: We have Adam Smith's writings.

MR. McCONNELL: Yes, they would have those.

THE CHAIRMAN: If you would like to put them in, we would be glad to have them.

MR. ODDLEIFSON: Perhaps in a slightly different way than Adam Smith wrote it, but basically the same.

THE SECRETARY: The summary, additional pertinent information, will be Exhibit 70, and Exhibit 71, Adam Smith's principles.

--- EXHIBIT NO. 70: Summary and additional pertinent information to the submission of Mr. and Mrs. E.W. Oddleifson and Mr. R.S. McConnell.

--- EXHIBIT NO. 71: Adam Smith's principles of taxation.

THE CHAIRMAN: Thank you, Mr. McConnell, for your summary. This is rather interesting in that it has certainly pointed out to us that a great resurgence of French economy is due to exactly the opposite of what you are recommending; namely, they have placed great weight on consumption taxes. Roughly 65% of their total budget is received in that way as opposed to about 35% in

5 Canada, and their economy moves forward very quickly. There may be other reasons for this, of course, and they raise a lot of their consumption tax money by way of value-added tax.

MR. McCONNELL: Yes.

THE CHAIRMAN: Which may not pyramid. I am not sure. I do not think it has a great pyramiding effect. By the way, I point out, sir, sales tax commenced in Canada about the year 1922 or 1923.

MR. McCONNELL: As far back as that?

THE CHAIRMAN: Right. We were one of the first countries who adopted universal federal sales tax.

MR. McCONNELL: One of the sad features about that is this: with those taxes levied at various points in the production pipeline, they compound themselves. One tax is built on another tax, and so on, so that by the time it reaches the eventual consumer, the tax has been multiplied - just as an illustration.

COMMISSIONER WALLS: Would you not get rid of pyramiding if the sales tax was moved forward to the retail level?

MR. McCONNELL: If they were left at the retail level?

COMMISSIONER WALLS: Would you get away, then, from pyramiding?

MR. McCONNELL: Yes.

THE CHAIRMAN: I think Mr. McConnell is directing himself to pyramiding of tax rather than to pyramiding of
2 profit on tax. I have never myself been concerned about pyramiding of taxes. It seems to me the fact that one tax

is imposed on something else which itself contains taxes simply means that the rate of tax is not stated in as high a rate as it would be if it were placed back on the original base.

However, I am very much concerned about something that is represented to us, that a great deal of the pyramiding of profits on tax, and if profits are greater because of consumption of taxes, the taxpayer is paying more than he would otherwise pay and the merchants are making more money than they would otherwise make. So we have asked merchants if that pyramiding were removed, if they would receive less profits. Do you think they would?

MR. McCONNELL: Perhaps this would answer your question, if I might deviate a little, but I will try to get back to it. This is from the Excise Tax Act: general sales tax of 8% is levied by the Government of Canada on the sale price of goods manufactured in Canada and on the duty-paid value of imported goods. This tax, together with an additional rate of 3% imposed under the Old Age Security Act, is payable at the manufacturer's level at the time of delivery to the purchaser or by the importer at the time of importation.

Well, I understand that that 8% tax levied on goods coming into the country is on top of the duty, whatever that might be, and then the 3% Old Age Security tax is on top of those two taxes, whatever they might be.

THE CHAIRMAN: That is not correct. The 8% and 3% are added together.

MR. McCONNELL: That makes 11%. Well now, let us say that the next step in the distributive chain might

be the wholesaler. Not in all cases, I know, because they do not always go through a wholesaler, but if they do the wholesaler would add his percentage markup to that, to the cost of the goods, plus 11%. He adds his markup, which is a percentage markup, I believe.

Then, he would pass it on to the retailer, and the retailer would add a percentage markup to that accumulated total. No doubt his profits, as you have suggested, are larger because of the taxes than they would otherwise have been. That is, if he has a fixed markup. Of course, I realize that our distributive machinery has altered greatly in the past generation, let us say. It is changing, but the principle is there. I think if anyone were to take a selected stage of goods and commodities and follow them through from the time they enter the country or from the time they are manufactured, follow them through right to the retail shelves, you would find the markup would be surprising.

THE CHAIRMAN: I have a pretty good idea what the markup is because we have asked those kinds of questions. The answers have left us, to some extent, unsatisfied as to whether or not any merchants have increased their earnings because if there is pyramiding obviously someone is making more money because of tax. I do not think we have been able to completely satisfy ourselves on that score, and I think we could only do that by a pretty factual statement as to what occurs when the tax is changed.

MR. McCONNELL: Yes. It is a little difficult to follow through. If we could realize what consumer taxes

are doing to us and doing to our economy, I think the people down at Ottawa would find some way of ameliorating the situation.

COMMISSIONER WALLS: I notice, Mr. McConnell, in your opening remarks you state that the sales tax had an adverse effect on Canadian industry in expanding abroad, or at least I understood you to say that. Now, surely that is not correct in that, first of all, there is no sales tax on the product that is shipped abroad, and secondly, there is no sales tax on the machinery or production in producing the product, so sales tax, really, has had no implication on any of our products that are exported.

MR. McCONNELL: You mean on our competitive position?

COMMISSIONER WALLS: That is right.

MR. McCONNELL: Yes, I would agree with that. I did not know that goods shipped abroad were exempt.

COMMISSIONER WALLS: I see.

MR. McCONNELL: So that would just leave the domestic field. That statement would apply, then, only to the domestic field.

COMMISSIONER WALLS: Yes, that is right. Then, on page 4, surely the inflow of capital from the United States does the very opposite of creating deficits in Canadian foreign exchange, as you mention. That is in the top paragraph on page 4. I would like you to explain why you feel this inflow of capital creates a foreign exchange deficit for Canada.

MR. McCONNELL: Is this the part referred to: "Seeking to escape the high taxes imposed in the United

9 States"?

COMMISSIONER WALLS: No, it is right in the centre. "They come to Canada, and although a measure of employment is created, they tend to pre-empt the field of Canadian investment. This leads to deficits in Canada's foreign exchange." Now, surely the inflow of capital has the opposite effect, does it not?

MR. McCONNELL: Well, that may be a bit ambiguous there. What I really meant was that the interest and dividends on this capital to be transferred later would affect our balance of payments. It would complicate our balance of payments. I am taking this from an American magazine, "Newsweek" - by the way it is rather uncomplimentary to our former Prime Minister.

I/PB/ss

Canada's total trade deficit with the United States is about seven million dollars a year. Above this is a further six million dollars paid out to the United States in the form of interest and dividends on American investments in Canada. That is what I referred to there.

COMMISSIONER WALLS: I see.

MR. McCONNELL: It was dividends on this capital.

COMMISSIONER WALLS: I just have one more question to ask you, and that is where you refer to sales tax being complicated administrative machinery. Now, it might be complicated. I don't see it is more complicated than others. Certainly it is about the most inexpensive method of collection. It is about one-half of one percent; our cost of collecting sales tax and excise tax in Canada,which is a great deal less than the cost of collecting our other taxes.

MR. McCONNELL: That is not large. I would have thought it would be much greater.

COMMISSIONER WALLS: No. We have the figures and that is the percentage. You will agree that that argument is not very valid where it shows it is the least expensive method of collection of tax.

MR. ODDLEIFSON: Is this one-half of one percent of 3%?

COMMISSIONER WALLS: One-half of one percent of the collection; in other words, it is $5.00 per $1,000.00 collected.

MR. ODDLEIFSON: Sales tax is 3%.

COMMISSIONER WALLS: Sales tax is 8%, Federal tax.

MR. McCONNELL: Federal is 8%.

COMMISSIONER WALLS: Plus excise tax of either or 10 or 15 %.

THE CHAIRMAN: It would be easier, perhaps, would it not, to determine the amount of sales and the amount of income, sales opposed to income.

MR. ODDLEIFSON: We feel that the percentage does not matter. It is the way it is collected and how it is collected, from whom, that it appears in the price of goods and as a result increases the price of the goods themselves. The amount is not a significant thing with us. It is the fact that it is there.

COMMISSIONER WALLS: I agree with that statement in part. My point was in the brief you stated it was complicated.

MRS. ODDLEIFSON: I think, perhaps, we were thinking in terms of what it does to the little merchant, the small grocer who has to put in the expensive accounting machinery. It must be a terrible headache.

COMMISSIONER WALLS: I think your simile is unfortunate, because food is exempt from Federal sales tax. The grocer wouldn't have to worry about that. In most provincial tax food is also exempt.

MRS. ODDLEIFSON: I am speaking of the small town where one store handles a lot of things.

THE CHAIRMAN: The general merchant.

COMMISSIONER WALLS: Fine.

MRS. ODDLEIFSON: And the antagonism it causes.

THE CHAIRMAN: You have a point, there is no doubt about it. It is a nuisance to the small merchant,

but I suspect income tax returns are a nuisance to him also.

MRS. ODDLEIFSON: When you can make it clear to people that they have to pay, it is equitable, I don't think anybody would object to paying for things that they owe, but to have things taken away from them, that they feel is not right. I see it from a woman's point of view, of course, and to me it is faulty housekeeping. If we keep using expedients to clean our house and let dust collect under the rug, eventually we are going to have to leave the house. I think any woman realizes worn out tools are not going to keep the house clean. If we are going to continue to use these things that are not doing the job, and are not making our individual homes happy places, something should be done about it.

THE CHAIRMAN: Your simile is apt if one accepts the views you put forward as to consumption tax.

MRS. ODDLEIFSON: I see the whole thing as a picture. I see it not only as tax inflating, but everything we do practically inflating and causing our dollar to die. Mr. McConnell sees it in a literary way. He writes a book. My husband, he is an engineer and he looks for scientific removal of the effect. I see it as a picture. I would be glad to show it to you if you would like to see it.

THE CHAIRMAN: I don't know whether I want to take the time. What is it that you wish to show?

MRS. ODDLEIFSON: I have a chart.

THE CHAIRMAN: Showing the effect of inflated tax?

MRS. ODDLEIFSON: Everything.

MR. ODDLEIFSON: A maze is what they call it.

THE CHAIRMAN: Would you hold it up?

---Mrs. Oddleifson shows Commission chart.

THE CHAIRMAN: I think that is very nice. Have you shown it to our press table?

MRS. ODDLEIFSON: I think you should be a woman really to see this. I think of it as tyranny of the tea table. We are too busy having pink teas and socials and so on. Ladies, I know they are necessary, but can't we cut them down a little.

THE CHAIRMAN: Thank you very much indeed.

MRS. ODDLEIFSON: You are welcome.

THE CHAIRMAN: I think you put something before us which is most interesting. We certainly don't wish to top it. I think it is a very good note on which to end this session. Thank you very much indeed.

MR. McCONNELL: Thank you for giving us the opportunity of presenting our brief.

THE CHAIRMAN: It was very kind of you to come.

MRS. ODDLEIFSON: Thank you for your interest.

THE CHAIRMAN: Mr. Secretary, do you have any further business?

THE SECRETARY: I want to enter one more brief into the record, the brief from Mr. Ronald Dorn, 82 West Humber Boulevard, Rexdale, Ontario. I will enter this brief into the record as Exhibit No. 72.

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---EXHIBIT NO. 72: Brief of Mr. Ronald Dorn.

THE CHAIRMAN: Thank you. We will stand over until Tuesday morning at 9:30.

THE SECRETARY: That is correct, and we will hear the submissions of the Ontario Credit Union League Limited and the Retail Merchants' Association of Canada.

---Adjournment.

ROYAL COMMISSION

ON

TAXATION

HEARINGS

HELD AT
TORONTO
ONT.

VOLUME No.: 24

DATE: May 21, 1963

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ROYAL COMMISSION ON TAXATION

Hearing held in Howard Ferguson Auditorium, Sir Daniel Wilson Residence of University College, University of Toronto, Toronto, Ontario, on Tuesday, the 21st day of May, 1963.

COMMISSION:

MR. KENNETH LeM. CARTER -- Chairman

MR. J. HARVEY PERRY

MR. A. EMILE BEAUVAIS

MR. DONALD G. GRANT

MRS. S.M. MILNE

MR. CHARLES E.S. WALLS

LEGAL ADVISER:

MR. J.L. STEWART, Q.C.

RESEARCH DIRECTOR:

PROF. D.G. HARTLE

SECRETARY:

MR. G.L. BENNETT

ROYAL COMMISSION ON TAXATION

HEARINGS HELD AT THE CITY OF TORONTO, ONTARIO

May 2I, I963

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Legemd (≠) Indicates page to and from

* (See Volume No. 24-A dated May 2I, I963 of The Royal Commission On taxation records of submissions.)

Toronto, May 2I I963

Ontario Credit Union League Limited.

Volume No. 24

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Ontario Credit Union League Limited

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Ontario Credit Union
League Limited

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Note: Supporting unabridged "Brief" as submitted by the participant is contained in Volume No. 24-A dated May 2I, I963 of The Royal Commission On taxation (Records of Submissions).

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Toronto, May 2I, I963

The Retail Merchants'
Association of Canada
(Ontario) Incorporated.

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The Retail Merchants'
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The Retail Merchants' Association of Canada (Ontario) Incorporated

Volume No. 24

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INDEX OF EXHIBITS

Toronto, Ontario,
Tuesday,
21st May, 1963.

EMT/dpw

--- On commencing at 9.30 a.m.

THE CHAIRMAN: Mr. Secretary, even though the clock has not yet reached half-past nine, if our visitors would like to start, I think we are all ready here.

THE SECRETARY: Mr. Chairman and Commissioners, this morning we have a brief from the Ontario Credit Union League Limited. The officers of the League are with us this morning. Mr. J.M. Hallinan is General Manager. He will speak to the brief and introduce his colleagues. I would like to enter this brief into the record as Exhibit No. 73.

--- EXHIBIT NO. 73: Submission of the Ontario Credit Union League Limited.

SUBMISSION OF THE ONTARIO CREDIT UNION

LEAGUE LIMITED

Appearances: Mr. J.M. Hallinan
Mr. C. Creswell
Mr. James Turley
Mr. John Burton

THE CHAIRMAN: Thank you, Mr. Secretary. Good morning, Mr. Hallinan and gentlemen. We have received your submission and have read it with a great deal of interest. We have some questions to put to you, and for that purpose we have asked our legal adviser and counsel, Mr. Stewart, to attend this morning. We have considered this a most important submission that you have made. We do not ask Mr. Stewart to lead the questioning in all cases; only those which we think are of great importance, or perhaps technically difficult. Under these circumstances

we wish to make sure that we have explored your submission fully.

Usually we ask our visitors if they care to say something before we start questioning. There is no need to read the submission. We have already done that, and it is entered into the record without reading. However, if you care to speak to it, summarize it or amplify it or anything that you please, we will be very glad to hear from you. In the meantime, Mr. Hallinan, would you care to introduce your associates in this matter?

MR. HALLINAN: Thank you, Mr. Chairman and Commissioners. On my extreme right is Mr. Clint Creswell, Supervisor of Examinations for the Ontario Credit Union League Limited. On my immediate right is Mr. James Turley, Director of Field Services for the Ontario Credit Union League. On my left is Mr. John Burton, Assistant Supervisor of Examinations for the League, and who has been chiefly responsible for the drafting of this submission.

I would like, first of all, to sincerely thank you for giving us the opportunity of sitting down with you this morning to go over our submission. We are prepared insofar as we are able to attempt to answer any questions that the Commission may have.

I have had the opportunity of reading the observations made by The Honourable Senator Vaillancourt and basically we are in complete agreement with the sentiments he has so ably expressed on the subject. I think in resume our brief indicates our desire to maintain the status quo in respect to taxation affecting credit unions in this province, in our League.

We have based our arguments largely on the reasons that we had in 1945 when the last Royal Commission on Taxation met. That Commission, as you know, unanimously recommended to the Government, and, in turn, enacted the tax law respecting credit unions. We are still of the opinion that the same principles obtain now as obtained then, and it is basically on that philosophical and sociological approach that we have made this submission, Mr. Chairman.

THE CHAIRMAN: Thank you, sir. We will ask Mr. Stewart if he will start our questioning. Mr. Stewart, are you ready?

MR. STEWART: Yes, thank you, Mr. Chairman. Mr. Hallinan, I wonder if you could indicate to the Commission at the outset how long you personally have been with the credit union movement?

MR. HALLINAN: I have been personally associated with this League since 1942. It would be a matter of 21 years. For the first five years it was on a voluntary basis either as Director or editor of the newspaper. Since 1947 I have been full-time manager of this League.

MR. STEWART: Now, I have before me a pamphlet or a booklet which is entitled Credit Union Year Book, 1962, and which appears, from the back cover, to have been issued by the Credit Union National Association, which I gather is an international organization with headquarters in Madison, Wisconsin. Are you familiar with that book?

MR. HALLINAN: Yes, I am, sir.

MR. STEWART: I observe on page 61 of the book you are mentioned as one of the Canadian organizations from

whom information about credit unions can be obtained.

MR. HALLINAN: That is correct.

MR. STEWART: And I observe, on page 60, that there is a chart with regard to the organization of the Credit Union National Association. I am sorry I have only one copy of this book and I should perhaps show you what I am referring to as I go along. This chart on page 60, which sets out the organization of the credit union movement in diagrammatic form says this at the bottom of the page: CUNA, which I take it is the abbreviation of Credit Union National Association ---

MR. HALLINAN: That is right.

MR. STEWART: --- is an association of leagues of credit unions; leagues are voluntary due-supported associations of the credit unions in any state, province, country or other governmental unit having its own laws.

Then there is a reference to CUNA Mutual Insurance Society and CUNA Supply Co-operative, and it states that these are service organizations affiliated with CUNA, the parent body. Now, is that a fairly accurate description of the structure of the movement?

MR. HALLINAN: Yes, it is, sir.

MR. STEWART: And your League, the Ontario Credit Union League, is one of these leagues which are associated in the national organization?

MR. HALLINAN: That is correct.

THE CHAIRMAN: Do you mean international or national?

MR. STEWART: They call it national, Mr. Chairman, but I think international would be better. Mr. Hallinan,

I see that there are references here to Australia, Caribbean, Central America, Ireland, the Pacific Islands and South America as well as Canada and the United States where, presumably, operations are carried on.

MR. HALLINAN: That is right.

MR. STEWART: Now, there is a great deal of information in this booklet, Mr. Hallinan, about the credit union movement in Canada. Would you say that in your opinion that information is basically correct?

MR. HALLINAN: Yes, I would say so.

MR. STEWART: Well now, this information does show, as I see it, that there has been a quite remarkable growth of the credit union movement in Canada in recent years, and I would like to refer to certain aspects of that growth as set out in this book.

I find, on page 52, for example, that if we take
2 the year 1945 as your starting point, in 1945 there were 2,219 credit unions in Canada, whereas in 1960 there were 4,413. It is about double the 1945 figure.

MR. HALLINAN: That is right.

MR. STEWART: And in 1945 there were 590,000 members, and in 1960 there were 2,544,000 members, which is over four times as many.

MR. HALLINAN: That is right.

MR. STEWART: In 1945 the savings in these Canadian credit unions aggregated $139,000,000, whereas in 1960 the corresponding figure is $1,194,000,000, which, of course, is over eight times as much.

MR. HALLINAN: That is right.

MR. STEWART: Then, if I go to page 54 of this

book I find that in 1945 the total assets of the Canadian credit unions amounted to some $45,000,000, whereas in 1960 they amounted to $1,299,000,000, which again would be - well, I think in this case it would probably be nine times as much. Is that also correct?

MR. HALLINAN: Yes, that is true.

MR. STEWART: On page 55, when we deal with the average savings for each member of the credit unions in Canada, in 1945 the figure was $235, and in 1960 it was $470, which is exactly twice as much.

MR. HALLINAN: Yes, sir.

MR. STEWART: Then, going back to page 52, in 1945, with 2,200 credit unions and 590,000 members, the average number of members would be something under 300 per credit union.

MR. HALLINAN: Yes.

MR. STEWART: In 1960, however, the number would have grown, the number per credit union would have grown to approximately 600 per credit union.

MR. HALLINAN: Yes, sir.

MR. STEWART: Now, when I go to the earlier part of the book I find some figures for 1961. On page 6 I find that in 1961 there was an increase of 174 in the number of credit unions in Canada.

MR. HALLINAN: That is correct.

MR. STEWART: In 1961 the aggregate membership of credit unions in Canada was just over 2,700,000. This is on page 7. It also appears on page 7 that in 1961 the percentage of the Canadian population which were members of credit unions was 14.7%.

MR. HALLINAN: That is the national average.

MR. STEWART: Yes.

MR. HALLINAN: I might just point out the Ontario average is a little below that of the national average.

MR. STEWART: Yes, I am going to come to Ontario, if I may, in just a minute, and I will be very interested in that figure. Then, again, looking at page 11 of this booklet, in 1961 the total assets of the Canadian credit unions amounted to $1,468,000,000.

MR. HALLINAN: Yes.

COMMISSIONER PERRY: Those figures would be as at the end of the year, would they?

MR. HALLINAN: Yes, they would.

COMMISSIONER PERRY: December 31st.

MR. STEWART: The witness says yes, Mr. Perry. Now, Mr. Hallinan, have you, by any chance, corresponding information as at the end of 1962, or is that ready yet?

MR. HALLINAN: The 1962 figures for Ontario are not available yet.

MR. STEWART: So that the figure for Canada would not be available either?

MR. HALLINAN: No.

MR. STEWART: Then going for a moment to your brief as filed, I would refer in particular to paragraph 14 where you indicate there that in 1949 there were 423 active credit unions in Ontario with total assets in excess of $21,000,000. By 1962 the number had risen to more than 1,450, with total assets of approximately $275,000,000.

I observe that the number of unions in Ontario has increased in that 13-year period to three times the

1949 figure, and that the assets have increased to about thirteen times the 1949 figure.

MR. HALLINAN: Yes.

MR. STEWART: Then, if I can go back to this exhibit, Mr. Hallinan - I am sorry, I called it an exhibit because I am going to identify this booklet as an exhibit for the purposes of this inquiry - looking at page 38 I find that particulars of the members of credit unions in Canada are broken down province by province, and there we find a figure for Ontario of 1,396 credit unions - this is in 1960 - with a total membership of 538,000, and I find in Quebec that there are 1,470 unions with a total membership of 1,339,000 people. Do you confirm those figures?

MR. HALLINAN: Yes, I do.

MR. STEWART: Now, could you perhaps give some explanation of the fact that the number of members in Quebec in 1960 was over two-and-a-half times as great as the number in Ontario?

MR. HALLINAN: The explanation I could give for that, sir, would be the fact that the Quebec figures include not only the English-speaking credit unions, but also Caisses Populaires, and in Quebec we regret to admit that they had about a 40-year start on us. Caisses Populaires in Quebec started by Desjardins in 1900, and grew very much more rapidly than in Ontario. In fact, the Ontario growth did not really commence until the passing of the Credit Union Act in 1938. It was just in the 22-year period from, say, 1940 until now - 23-year period - that the credit unions have taken on.

MR. STEWART: It has been suggested to me that

the credit union movement in Canada in the early years, and I suppose this statement may relate particularly to Quebec, consisted of small rural credit unions. Would you indicate whether or not you would agree with that statement?

MR. HALLINAN: From my knowledge of the situation, sir, that would be substantially correct.

MR. STEWART: I take it, then, from what you said that you would not anticipate that the larger number of members in Quebec will continue; that you would anticipate that membership in Ontario will gradually overtake that in Quebec?

MR. HALLINAN: I would think so, judging by the development in this province during the past ten years. I might point out, in explanation of that, that the development in Ontario, according to the figures in paragraph 14, has been largely in the industrial credit unions, whereas, as you have suggested, the development in Quebec has been largely rural.

Another thing that would help to increase the credit union movement in the industrial area in this province is the continuing growth of industry, and the thing that would militate against the development of community-type credit unions in Ontario is the arbitrary figure of 6,000 that the Department of Insurance in this province have set as maximum potential that they will grant a charter.

B/MC/ss

MR. STEWART: Thank you very much. Now, in this Credit Union Yearbook I find some other figures which I would like to ask you to confirm or otherwise. On page 56, which relates to Canada, there is a break-down of installment credit by types of institutions. The first year quoted on here, the first year for which figures are given, is 1953, and the last year is 1960. Then the figures are given for six different types of institutions: The sales finance companies, the small loan companies, the department stores, other retail dealers, chartered banks, personal loans and the credit unions.

I observe from this that for a period of seven years the loans by the sales finance companies have increased from $516,000,000.00 to $828,000,000.00; those by the small loan companies from $176,000,000.00 to $544,000,000.00. I think I might observe in passing that in the case of the sales finance companies that seems to represent about a 60% increase; in the case of the small loan companies the increase is about 200%. Then in the department stores the 1953 figure is $167,000,000.00, and the 1960 figure is $368,000,000.00, which seems to be an increase of about 120%. The other retail dealers have gone up from $516,000,000.00 to $670,000,000.00, which is an increase of about one-third. The chartered banks have gone up from $308,000,000.00 to $857,000,000.00, which is something under 200% increase. The credit unions have gone up from $129,000,000.00 to $425,000,000.00, which is an increase of roughly 233%, and is the largest percentage increase from the 1953 figure.

Would you agree with that?

MR. HALLINAN: Yes, I would.

MR. STEWART: And in 1960, credit unions supplied 11.5% of the installment credit supplied by this group of institutions throughout the country. Is that correct?

MR. HALLINAN: Yes.

MR. STEWART: Now then, Mr. Hallinan, I have not been able to find this figure in this pamphlet issued by the Credit Union National Association, but I have been informed that in 1961 the personal savings of Canadians were divided among four types of institutions somewhat as follows: The four types I have in mind are the chartered banks, the trust and loan companies, the savings banks, and the credit unions. The figures that have been supplied to me indicate that 75.1% of personal savings were in the chartered banks, 6.8% in the trust and loan companies, 4.9% in savings banks, and 13.2% in credit unions.

Now, it is perhaps unfair to ask you to agree or disagree with those figures, but as far as the credit union operation is concerned, that is 13.2% of personal savings, would you think that was approximately correct?

MR. HALLINAN: From any information I had, sir, I would suggest that it would be approximate.

MR. STEWART: Thank you very much. Now, looking again at your brief, Mr. Hallinan, I now have before me paragraph 46, which is on page 16. You indicate there that the normal rate of interest charged by the majority of Ontario credit unions is 1% per month on the unpaid balance

of a loan. Is that correct?

MR. HALLINAN: That is correct, sir.

MR. STEWART: Could you tell me what the effective rate per annum is of 1% per month on the unpaid balance.

MR. HALLINAN: Could I have the permission of the Chair to ask Mr. Burton to supply that information?

THE CHAIRMAN: Yes.

MR. BURTON: Is that compounded?

MR. STEWART: No, simple.

MR. BURTON: It is approximately 12% per annum simple interest.

MR. STEWART: Is simple interest what we should be taking into account then?

MR. BURTON: 6.5% on the principal if repaid monthly installments in one year. There is a comparison with the banks' usual 6%.

MR. STEWART: The usual charge is one-half of 1% above the bank rate of 6%?

MR. BURTON: Taken on the principal, that is correct, yes.

MR. STEWART: You also indicate in paragraph 69 of the brief, and I am looking at the top of page 25, that you do pay a rebate. In 1961, the average rebate paid by Ontario credit unions was approximately 16%.

MR. HALLINAN: That is correct.

MR. STEWART: Now again, if we were trying to determine the effective rate on loans made to people who got that average rebate, do I take it that we would reduce the 6.5% by 16%?

MR. HALLINAN: That is correct.

MR. STEWART: And then for the members of your credit unions who paid the 1% per month and obtained this average rebate in 1961, the effective interest rate would be something under 6%.

MR. HALLINAN: Yes.

MR. STEWART: It would be approximately, I suppose, 5.5%.

MR. BURTON: Yes, that is correct, Mr. Stewart. Some credit unions don't pay any rebate and another credit union might pay as much as 25 or 30. A 10% rebate would bring it down to less than the general bank rate of 6%.

MR. STEWART: Of course, when we talk about the bank rate as being 6%, that is the maximum rate that the banks are permitted to charge.

MR. BURTON: Yes.

THE CHAIRMAN: Mr. Stewart, I am not very clear on the relationship between 1% per month and 6½% per year and it may be that my multiplication does not work fast enough to comprehend it. On a loan of $100.00, as I understand it, the payment might be $1.00 per month average of twelve months, or in all throughout the year, the borrower would have paid $12.00. Now, I don't think that is equivalent to $6.50 at the end of the year.

MR. BURTON: The interest works out $1.00 per hundred, or 1% per month on the reducing balance. If you borrowed $100.00 from the credit union and repaid it in twelve equal monthly installments, you would finish up paying $6.50 interest based on a 360-day year.

THE CHAIRMAN: $6.50 is the payment one makes for obtaining $100.00 at the beginning of the year, which $100.00 is paid for fully at the end of the year by equal payments of capital monthly.

MR. BURTON: In other words, you will pay $6.50 for use on an average of $50.00 throughout the year.

MR. STEWART: At the beginning of the year, do you receive $100.00, on the Chairman's example, or $100.00 less a pre-payment for the first month?

MR. HALLINAN: You receive $100.00.

THE CHAIRMAN: Your comparison with the bank rate is not altogether valid, Mr. Stewart. You were talking of a bank rate that would be 6% on non-reducing balance. Is that correct?

MR. STEWART: That is correct, although I am not quite sure how these gentlemen reached that 6% figure which is, as I said, the top figure which the banks can charge. Perhaps Mr. Burton could explain.

MR. BURTON: Yes, I think I can clarify it by referring to recent advertisements in the Toronto papers by the Bank of Nova Scotia and the Toronto Dominion Bank and I believe that other banks are offering the same service which is a fully-insured loan. As an example, the Bank of Nova Scotia advertises you can borrow $1,000.00 for one year and you pay back in total, this is not a discount loan, you pay back $1,060.00. In other words, going back to the other illustration of $100.00, instead of paying $6.50 you pay $6.00. There is the bank's 6%.

COMMISSIONER WALLS: You are paying $60.00 on an average of $500.00 loan throughout the year.

MR. BURTON: From the bank, and $65.00 on $500.00 average from the credit union.

THE CHAIRMAN: I understand, Mr. Burton.

MR. STEWART: I would like, if I may, Mr. Hallinan, to look at Appendix 4 to your brief so that I can be sure I understand exactly what appears there. On the second page of that appendix it appears the expenses which you specify for the year 1961 amounted to 36.9% of the gross income of the unions whose returns are reflected in this chart. Is that correct?

MR. HALLINAN: Yes.

MR. STEWART: And your net income therefore was 63.1% of your gross income. I was curious to know why it was that you stated on the next line, the next line salaries and Honoraria as a percentage of total expenses and the overall figure is 28.4%. What significance is there to that in your thinking?

MR. BURTON: This last line on page 2 was merely for the guidance of our credit unions. In the last few years as they have grown large enough to employ full-time personnel they have often wanted to know how much they should pay out in salaries, how much they could economically pay out in salary and Honoraria and we have set a general rough guiding line as not more than 20% of gross income, or not more than 50% of expenses, regarding those as maximums. That was the only purpose for including that.

MR. STEWART: Thank you. And now then, I look at Appendix 3 to your brief and I realize, of course, that Appendix 3 contains statistics which were prepared by

the Ontario Department of Insurance, whereas Appendix 4 sets out statistics for members of your League. However, I take it that broadly speaking if we want to follow through what happens to the net income of your Credit Unions, and I am referring now to the 63.1% in Appendix 4, we can find that roughly from Appendix 3. In other words, about just halfway down Appendix 3 I find the figure for income $21,800,000.00 odd and then I find expenses of $9,300,000.00 and net earnings of $12,489,000.00.

Now, before I go further, I take it that the $9,392,000.00 on Appendix 3 corresponds generally to the 36.9% which I refer to on Appendix 4. Is that correct?

MR. BURTON: Yes.

MR. STEWART: So that when we want to determine what happens to the 63.1% we then look further down Appendix 3 and we find that 20% goes to the guarantee funds and then there is a figure of $8,900,000.00 odd which goes back to the members in one form or another. That appears to be, according to my calculations, about 72% of that net income and then there is another million and sixty-five thousand dollars which is added to the other funds and reserves. Is that the general picture?

MR. BURTON: Yes, Mr. Stewart. Maybe we should just clarify one point. There is a little difference between these Government statistics and our own statistics on Appendix 4. On Appendix 4 it is indicated that these are statistics for 1,236 credit unions, whereas the Government's statistics are based on reports of 1,315.

One of the reasons is there are a few French-speaking credit unions which are not members of our League. Therefore we don't include their statistics. There are also seventy-odd Caisses Populaires.

T/dpw

In Ontario only three or four of them are members of this League. Most of them are in the French-speaking north, and if you have seen the statistics of the Caisses Populaires in Quebec, you will realize they might change our statistics from the Government statistics which includes some Caisses Populaires. Apart from that we would agree with you.

MR. STEWART: Thank you, Mr. Burton. I am really at the moment just attempting to make sure that I understand the general application of these funds. At the bottom of Appendix 3 you deal with the type of disposition which may be made of the figure of 1,065,000 dollars, and there are four possible uses referred to. One is donations, one is educational funds, one is other funds and reserves, and the last consists of honoraria to officers who are not paid out of expenses. Can you tell me what is the amount of educational funds on that list?

MR. BURTON: Yes, Mr. Stewart. As referred to in the brief, paragraph 31, on page 11, the section of the Credit Union Act reads:

> "A credit union may by resolution of the members provide that, after making provision for the guarantee fund and before declaring a dividend, an amount not exceeding 5% of the net earnings be set aside in a special fund to be used for such educational purposes as are specified in the resolution."

In other words, a credit union may set aside 5%

of its net earnings after providing 20% guarantee fund reserve for educational purposes. These are not, in this case, charged as an expense but are set aside out of net earnings.

MR. STEWART: What do you mean by "educational purposes"?

MR. HALLINAN: There are two phases, Mr. Chairman. One is educating the present membership to the many advantages of using the service of the credit union. That is a program that increases the membership of the credit union and makes the members make better use of it.

Another phase in our educational program, which is rather recently introduced, is known as the family financial counselling. Programs are put on for the benefit of members, teaching them how best to use their money. The other aspect of the educational fund in a credit union would be to spend funds in programs that would induce people that are eligible for membership in credit unions to take out membership in the credit union. They are the basic purposes of the educational fund of credit unions.

MR. STEWART: Basically these monies are used to maintain your present membership and, if possible, increase it?

MR. HALLINAN: That is correct.

MR. STEWART: Looking at Appendix 3, I observe that the first item under liabilities and members' equities is shares, and that the amount shown opposite the word "shares" on this statement, and I appreciate this is not your statement; it is a governmental statement - that the amount is $183,583,300.

Now, have you any idea, either as regards the credit unions whose affairs are reflected here or as regards those which are members of your League, what proportion of that $183,000,000 represents original subscriptions for shares by members and to what extent it represents dividends?

MR. BURTON: Mr. Stewart, I do not think we have any idea to enable us to answer that question intelligently.

MR. STEWART: Do I understand your procedure to be that the dividends that you do pay are basically credited to the members' accounts?

MR. BURTON: That is correct, yes.

MR. STEWART: And if, therefore, I am a member of a credit union and I have subscribed for a particular number of shares, and at the end of my first year of membership I am credited with a dividend, does the number of shares I hold increase or is the amount which is to the credit of my share account simply increased?

MR. BURTON: The dividend is credited to your share account. The share value is $5, but they are not shares in the same way as another corporation. If you have $52 in the share account, you have ten $5 shares and $2 subscription towards the eleventh. If you get a dividend on that of, shall we say, $2, it increases the amount to $54. You still only have ten shares but you have $4 on subscription towards the eleventh share.

This division into shares is merely convenience. There is no certificate. There is nothing in the same sense as another corporation.

MR. STEWART: In effect, if, through payment, I

subscribe for ten shares for a total of $50, and without any further subscription on my part, the amount of the credit of my share account increased to, say, $80, I would, in effect, be treated as owning 16 shares in the credit union?

MR. BURTON: Yes, certainly. I might point out, if you wished at any time to withdraw any of the share dividend money credited to your share account, you would be entitled to do so. Some credit unions do do it; some of the larger ones may do it for university and community purposes.

MR. STEWART: The next item in Appendix 3 under that heading of liabilities, is deposits, and that amounts to about $47,000,000. That figure of $47,000,000 is roughly one-sixth of the total liabilities shown of $266,000,000.

Would that percentage of deposits have been fairly constant over the last few years, or has the percentage of deposits increased or decreased in Ontario in relation to total liabilities?

MR. BURTON: I would say that it is increasing a little, and although it is an irregular pattern, if you refer to Appendix 4 you will find some of the large credit unions running into the three million group have a much higher percentage of deposits than the smaller and the much larger credit unions. Generally speaking, there may be a slight increase, but not spectacular.

MR. STEWART: On these deposits I observe from paragraph 23 of your brief that if a deposit is what you call a regular deposit, you pay, or your unions pay, from

three to five per cent, and if it is a deposit for a personal order, the rate varies from nil to 3%.

Would you mind explaining to me what that second type of deposit is? What is a deposit for personal order?

MR. BURTON: Well, a credit union that wishes to provide personal chequing service, such as a bank provides, the member, in addition to his share account, may have a deposit account on which he can draw cheques.

MR. STEWART: I see.

MR. BURTON: And the amount he has sometimes has interest allowable upon it, and sometimes not, but this is a strictly personal chequing service which exists in comparatively few credit unions in Ontario.

MR. STEWART: Looking again at Appendix 3 there are three items, and the last three items of liabilities, guarantee fund, other funds and reserves, undivided earnings, which appear to amount to approximately $24,000,000, are roughly 9% of the liabilities.

Would it be fair to say that these three items are, in fact, reserves for the benefit of the membership as a whole?

MR. HALLINAN: I would say definitely yes. The guarantee fund particularly, which is by far the largest of the reserves, is set up to offset any possible losses on loans to members, thereby affording a protection to the general membership.

The other funds in reserves, the educational one has been explained, and some credit unions looking towards the day when they would purchase their own building, have set up building reserves, and then the balance of the

net earnings, of course, are distributed pro rata to the membership.

MR. STEWART: When we come to this question of dividends, Mr. Hallinan, is there a normal rate of dividend which the Ontario Credit Union attempts to pay?

MR. HALLINAN: Yes, I would say that the average is around 4%. It has increased slightly over the past year. I remember about 20 years ago the average dividend paid was about 3½%. In more recent years I would suggest the dividend would hover slightly above 4%.

MR. STEWART: Then I gather from paragraph 45 of your brief, which is at the bottom of page 15, that after you provide for your 20% guarantee fund, you then determine what dividend can be paid. Let us take the dividends first. Does the determination of the dividend rate precede any provision for rebate on loan interest?

MR. HALLINAN: Not as a general rule. The Board of Directors of a credit union, after they have set aside the statutory reserve, usually draw up a resolution to be recommended to the annual meeting, and it usually includes the recommended dividend and the interest rebate.

MR. STEWART: So that the two come more or less contemporaneously?

MR. HALLINAN: That is correct.

MR. STEWART: I asked that question because you do say in paragraph 45 that a credit union pays a reasonable return on the members' savings, and if there are sufficient net earnings remaining, makes a rebate of loan interest.

MR. HALLINAN: Yes. Well, that can be explained by the fact that the Board of Directors of the credit

union makes a resolution. Now, in the preparation of that resolution, the Board would say, "Well, all right, a fair return would be, say, 4%. Now, if anything is left over, what amount of rebate may we offer?" It is the Board that decides that before it brings a resolution to the annual meeting.

MR. STEWART: As far as your deposits are concerned, you start off with a particular rate, and the rate of interest you pay depositors does not vary from then on.

MR. HALLINAN: It is at the pleasure of the Board of Directors. The Board of Directors has the authority to set the interest rate that the credit union will pay on deposits. Now, they may vary it from time to time.

MR. STEWART: Yes, but I may not have made my question plain. Let us suppose that the Board of one of your credit unions is dealing now with the results of operations for 1962, and it finds it has certain net income available, and it sets aside this amount for the guarantee fund. Then it will determine a rate of dividend for 1962. It may determine a rebate on loan interest for 1962, but does it also consider its own sort of retroactive increase in interest on deposits for 1962?

MR. HALLINAN: It could, but that is not generally so. Usually the interest on deposits is determined early in the year.

THE CHAIRMAN: You are not moving on, Mr. Stewart? Have you finished with that?

MR. STEWART: If you have any questions, Mr. Chairman.

THE CHAIRMAN: I have a question at this point. I understand that this meeting of the Board of Directors at the end of the year is to decide and it does decide the distribution of the net earnings as between shareholders and borrowers. In fact, very seldom does it make any adjustment on deposit accounts. What are the general considerations which a Board takes into account in coming to its conclusions as to the distribution? I would have thought that would be rather difficult, and I would like to know what are the usual determinants which the Board would consider?

MR. BURTON: If I may answer that, Mr. Chairman, one of the considerations, of course, is the past. Shall we pay 4% this year or shall we pay $4\frac{1}{4}$%? Another consideration is the relationship between the borrower and the saver, and it may well be if a credit union does not have sufficient borrowers, in other words it has surplus money, then it may consider an increased rebate on loan interest to encourage further borrowing, or if it is the other way around, if they have no trouble getting money out and can't get enough money in, they may say, "Let's give a higher dividend this year and keep the rebate down," and try and encourage savers.

They try to balance the situation up because the ideal is always to loan out just what your members put in; not to have to borrow or to have too much surplus. These are the main factors I would think.

THE CHAIRMAN: Mr. Stewart, I let you get beyond the statutory reserves, and I had a question on that which I think I should have injected at that time, perhaps. The

20% guarantee fund established by statute continues, apparently, indefinitely to accrue at the rate of 20% of income.

It occurs to me as this goes on it could well exceed the assets if it is in no way related to the assets.

MR. HALLINAN: If I may answer that, there is provision in the Act which says that once a guarantee fund equals 10% of the assets of the credit union, the credit union, in that year, is not required by law to set aside the 20%.

THE CHAIRMAN: Thank you.

COMMISSIONER GRANT: I noticed: last year, you increased your guarantee fund by about 27%. The allotment of 20% of your loans came to $2,497,975 which is about 27% increase.

MR. BURTON: Yes. Of course, we do not know here the amounts which may come to be written off out of that increase. The increase is 27%, but at the end of the next year quite a bit of that increase may have been written off from bad debts.

MR. STEWART: May I just ask a question about that 27% figure? At least, I understood Mr. Grant to say 27%, and the figure of $2,497,975 appears to me to be 20%, not 27% of the 12,489,000.

COMMISSIONER GRANT: I am referring to the guarantee fund, the nine million.

MR. STEWART: Yes, I see. That is, however, the aggregate reserve in the guarantee fund, not the amount that was allocated in respect to 1961.

D/MC/ss

COMMISSIONER GRANT: I see in 1961 it was increased by $2,497,000.00, which is 27% of the total.

MR. STEWART: I see. I beg your pardon.

COMMISSIONER GRANT: Which struck me as being a rapid increase in one year. I was wondering if that was to be maintained, my thinking was along the lines of the Chairman, that fund could go to a very large figure.

MR. BURTON: My answer to that, Mr. Grant, may be a better guide would a percentage of outstanding loans. Although the guarantee fund has grown that much, the total loans in the credit union have also grown in the year. Appendix 4, at the foot of the first page, we show the guarantee fund as percentage of shares and deposits and also as a percentage of loans. One is 4.68% and one 4.69%. It may be that the guarantee fund was a little low and now it is being brought up to a more normal percentage. As Mr. Hallinan pointed out, there is provision against the guarantee fund becoming too large.

COMMISSIONER GRANT: Have you the figuresto the end of 1962? We just have them for 1961. Have you any figures as to what the total loans were at the end of 1962?

MR. BURTON: No, they are being processed now. They are not yet available.

MR. HALLINAN: They are likely to be available in September. We have some university students that come in the Summertime and work on statistics for us.

THE CHAIRMAN: Would this be a good time to break off? I have a telephone call to make, and I would like to break some time in the morning.

MR. STEWART: As you wish.

THE CHAIRMAN: I would prefer it now if it would suit all concerned.

---The Hearing was adjourned for ten minutes.

THE CHAIRMAN: Will you continue, Mr. Stewart.

MR. STEWART: Thank you, Mr. Chairman. Mr. Hallinan, there is one other subject on which I would like to get some information from you as to facts. Perhaps we can turn to page 26 of your brief, the paragraph beginning about halfway down the page where you deal with the question of delinquent loans.

Now, you say there at the end of 1961 there were delinquent loans aggregating about 5% of loans outstanding and that roughly $2,300,000.00 of those loans, or 1.1% of loans outstanding, were in default for more than six months, six months or more, and loans aggregating $574,000.00 were written off during the year.

Now, I would like to refer you to this pamphlet issued by Credit Union National Association, and in particular to page 30, where this statement is made:

> "Because of their very nature as well as their safeguards, credit unions have an outstanding record of safety. Especially remarkable is the repayment of personal loans which are the credit unions' chief investment. Less than one-fifth of one percent of these loans prove uncollectable based on the experience of many years. The members honour their obligation to

their fellow members."

Now, are you suggesting in your brief that the experience in Ontario is essentially different from the experience that is reflected in that statement?

MR. BURTON: No, Mr. Stewart, I think the apparent discrepancy there is accounted for by this fact that the reference in our submission that 1.1% of loans outstanding had been delinquent for six months or more, part of the explanation could be that we are calling a loan seriously delinquent on which no amount of principal has been paid for six months or more, but in many cases payments of interest could be made. In some cases all the interest could have been paid and a large proportion of the loans which are delinquent six months or more in given time are ultimately collected or very seriously reduced.

We would say our experience in Ontario is quite average. We haven't any exact figures, although individual credit unions do in some cases. That is the explanation.

MR. STEWART: Now, I would like to go back to page 20 of your brief and I find there in paragraph 56 you set out certain quotations from the report of the Royal Commission on Co-operatives which made its report in 1945. Now, I think from the figures that were quoted from the booklet earlier it would be clear that in 1945 the assets of credit unions in Canada were approximately 10% and the number of members of credit unions in Canada was approximately, let us say, 20% of the corresponding figures for today. Is that fair enough?

MR. BURTON: That is right.

MR. STEWART: And I think you mentioned that in Ontario this type of organization became practically possible only in 1938, so between 1938 and 1945 I suppose the movement in Ontario was just getting off the ground?

MR. HALLINAN: That is correct.

MR. STEWART: Now, we have also I think agreed from this pamphlet that at the present time credit unions are supplying about $11\frac{1}{2}\%$ --- when I say at the present time, I mean at the end of 1961 --- credit unions were supplying about $11\frac{1}{2}\%$ of the installment credit of this country and they held about 13.2% of the personal savings of Canadians. Is that correct?

MR. HALLINAN: That is right.

MR. STEWART: Well then, Mr. Hallinan, I would be interested in your comment on this: Having regard to this growth which has occurred and to the percentages of installment credit and personal savings which credit unions represent today in Canada, have they not become a very significant element in the financial life of Canada and are they not in fact actively competing with the banks and other financial institutions for the deposit of the small saver and for the consumer-type loans?

2 MR. HALLINAN: That is a very good question, sir. I would suggest in answer to the first question we do believe that the credit union movement is playing a very significant part in the economy of this great country. In answer to your second question, we would rather look on it as other financial institutions competing with us.

MR. STEWART: In any event, there is competition.

MR. HALLINAN: Depends which way you look at it. We feel by organizing credit unions and their very tightly knit bond of association, people create a measure of economic security, being able to do it for themselves and by themselves. It is what other financial institutions up until recently were not able to do. Until recent years the Chartered Banks showed no interest whatever in personal loans. Added to that the Credit Union movement, through the institution of its own mutual insurance society has been able to provide loan protection and life savings insurance for the members. Many years afterwards, when other financial institutions saw that we made a success, they are coming into it. Very recently the banks gave that loan protection insurance. I understand some of the Trust Companies are offering premium life insurance on their savings.

We feel now as we did in 1945, that the reasons that prompted the Royal Commission of that date to make the observations they did then are just as valid today. We believe credit unions are performing a highly useful function in assisting people who are unable to take effective advantage of savings and loan facilities provided by other lending institutions.

MR. STEWART: One of the portions of the 1945 report which you quoted at the bottom of page 20, Mr. Hallinan, is this: "We" --- that is the Royal Commission of 1945 --- "...are satisfied that that the credit unions perform a highly useful function in assisting people who are unable to take effective advantage of savings and loan facilities provided by other lending institutions."

Now, is it not the case now that there are more alternative sources of loans available to the small man than there were in 1945?

MR. HALLINAN: I think that is a fair statement.

MR. STEWART: Is it not also the case that if the small man wishes to place his money out on deposit or loan he is not lacking in facilities at the moment outside the Credit Union movement?

MR. BURTON: Well, it is true, Mr. Stewart, that there may be more facilities for the small man now, particularly as Mr. Hallinan said, because they have had to raise the sights in the small loan field and the insurance field on loans and savings. There is still quite a bit true in these words from the Royal Commission in 1945. For instance, if many of our new members were to go to the bank for a loan, the bank which offers an insured loan at a slightly less cost than the credit union, if he has not been in his present employment for two years very likely he won't get the loan. In the bank's advertisement they have six boxes for check marks and if you can put "Yes" to each box, you can be reasonably sure you are eligible for a loan.

Therefore, to us it means it is much harder for a credit union member to obtain a loan from that bank than from his own credit union where he would not have to pass those six tests. There is still quite a lot of validity in the co-operatives' contention back in 1945.

As far as the finance companies are concerned, the rates, of course, are generally quite a bit higher than

the credit union.

MR. STEWART: Let me put this to you, because what we are here for essentially is to get your reaction to questions of this nature. If it is the case, as it appears to be, that the dividends and interest you pay your shareholders and depositors are more or less comparable with the rates of return they could obtain elsewhere on shares and loans or deposits, and if what you charge for loans you make to others is also comparable with rates of interest charged by other forms of lending institutions, then if you are not paying the taxes which they do, are you open to the suggestion that your operations must be less efficient than theirs?

/ET/dpw

MR. BURTON: I don't quite get the point of the question.

MR. STEWART: Let me rephrase it. If there is another type of institution whose shares one of your members can buy from which he will get approximately the same rate of dividend return he gets from you, if there is another type of institution in which he can deposit his monies if he wishes to, from which he gets more or less the same rate of return as he does from you, by the same token if there is a borrower and he can borrow from some other institution at very much the same rate as he borrows from you, now that other institution, let us assume, is paying tax at the ordinary corporate rate. You people, at the moment, are not paying tax at all.

Now, it seems to me, as I say, that it is a pertinent question and certainly it is one on which I would like to get your reaction. If these other people can absorb the corporate tax and still compete with you both on what comes in and what goes out, so to speak, are you operating as efficiently as they are?

MR. BURTON: I think the answer to that, Mr. Stewart, may be that in some of the smaller credit unions the operation might not be so efficient, but certainly with the larger ones it is probably just as efficient as the small loan companies. Of course, as far as the small loan companies are concerned, they are presumably able to pay a good return to their investors, but their loan interest rate, on the average, is considerably higher than the average credit union, and again you really have to separate the smaller and larger credit union because many

of the larger credit unions are actually returning 20 or 25 or even more per cent of the interest charged to members, which in some cases reduces it to 4 or 4½ per cent compared with the banks' six. Therefore, the borrowers are getting a much better deal. It is a demonstrable fact in the very large credit unions in Ontario, and I speak for them generally, the larger they get the more efficient they operate. Their expense ratio to gross income is much lower, and they can often return maybe 5% on shares and 25 to 30 per cent on the interest, so I think you must differentiate between the small struggling credit union just trying to serve its small number of members as efficiently as possible and the bigger credit union which has a full-time paid staff.

Many of the small credit unions work purely on a voluntary staff basis, so naturally you do not get such an efficient operation. I think that would be your answer.

MR. STEWART: Thank you very much, and if time permits I will come back to that. Let me ask you this: in what way does a credit union differ from a service co-operative?

MR. HALLINAN: I would say one big difference, Mr. Chairman, is that a credit union is limited to dealing only with its own members. It is not permitted by law to deal with the public generally. That, in my opinion, is what the basic difference is.

MR. STEWART: Of course, a service co-operative does not have to go outside its own membership, does it?

MR. HALLINAN: But I think one of their

principles is open membership, and in a credit union there is no such thing as open membership.

MR. STEWART: Well now, Mr. Hallinan, what I was leading up to with that question, as you can imagine, is this: if the operations of a credit union are essentially the same as those of a service co-operative, why should credit unions not be taxed in the same way as co-operatives?

MR. BURTON: By a service co-operative you mean the co-operative ---

MR. STEWART: Which provides a service of one kind or another to its members.

MR. BURTON: You include there a trading co-operative dealing in production and distribution?

MR. STEWART: No, I do not think that type would be called a service co-operative.

MR. BURTON: You are referring to the like of the medical co-operative?

MR. STEWART: I suppose that would be an example, yes.

MR. BURTON: Is it not true that the medical co-operatives are exempt from tax? I am not certain of this, but I believe the true service co-operatives are often exempt under the Income Tax Act.

MR. STEWART: Without deciding that, let me just see if I can give you some other suggestions as to what would be included under the expression "service co-operative."

THE CHAIRMAN: Are you seeking a definition of a service co-op?

MR. STEWART: Well, in effect, yes, or examples

of it.

THE CHAIRMAN: I think Mr. Walls can give you one very quickly.

COMMISSIONER WALLS:If by this type of co-op you mean one that the recipient of the patronage refund is taxable, is one that is incorporated and servicing a line of business that the members are in. That is probably not the clearest wording, but I mean it is selling produce for which the man depends on his livelihood, and that is the type of co-operative where a recipient pays tax on patronage dividend.

MR. HALLINAN: Any credit union dividend received by the members is taxable in the member's hands.

MR. STEWART: I agree.

MR. BURTON: If that is the definition of service co-op, is it not true that business is not confined to the membership? The business may be confined to the membership as far as buying produce of the growers, for instance, but it is not confined to the membership as regards the selling of that produce through the co-operative.

COMMISSIONER WALLS: It is only a co-operative selling the produce of the grower.

MR. BURTON: But it is selling to the public.

COMMISSIONER WALLS: Or selling to the wholesaler or selling to whichever medium of trade, but it is a co-operative selling the produce of its members.

MR. BURTON: So we would point out an important difference here between the service co-operative and credit union. A credit union deals solely with its members. It

receives money from its members and it loans to its members whereas the service co-op receives produce from its members but then it sells them to all and sundry according to the type of co-operative it is.

MR. STEWART: Mr. Chairman, I think I might read another definition of service co-operative. I take this from the booklet entitled "Recent Growth in Canadian Co-operatives," published by the Canadian Tax Foundation in 1962. That book contains three articles, the second of which is entitled "Postwar Taxation on Canadian Co-operatives," and was published in 1959.

At the bottom of page 3 of the second article I find this statement:

> "The group listed as service co-operatives represents a miscellaneous collection of activities including housing, rural electrification projects, medical insurance, transportation, recreational facilities, telephones, restaurants, frozen food lockers, boarding houses and other activities including the operation of farm machinery and farms."

Now, I am not sure, Mr. Chairman, if Mr. Walls would agree with that list or not.

COMMISSIONER WALLS: I am sorry, I was not listening. I was looking it up to get the exact quotation of what I just said and I was not listening. I apologize.

MR. STEWART: Not at all. I do not know that this is too important, but perhaps you could glance at this sentence and let me know if the co-operatives referred to there are service co-operatives under your understanding

of the term.

COMMISSIONER WALLS: Yes. Perhaps I should clarify my position. What you have got here and what you quoted as an interpretation of service co-operatives is quite correct. What I thought that you were attempting to get at was the type of co-operative on which it is demanded that on the patronage dividend the recipient is taxable, and the two are not necessarily the same thing.

MR. STEWART: No, I quite agree. I think we are on common ground, Mr. Walls. In the case of the credit union the dividend paid to the member is taxable just as patronage dividend is in the case of a co-operative.

What I am suggesting to you for comment is that a credit union may perhaps be regarded as a co-operative which is providing a particular type of financial service to its members, and do I take from what you have said so far that the only distinction you would draw between a credit union and a service co-operative is that a credit union confines its operations to its own members?

MR. BURTON: So do many of the service co-operatives. The medical co-operative, the housing co-operative
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- both of them are tax exempt and confine their operations to membership only.

MR. STEWART: Some of these other so-called service co-operatives, I take it, are not tax exempt?

MR. BURTON: No. Trading co-operatives and so on are taxable.

MR. STEWART: Do you suggest as you confine your operations to your members only, this differentiates you from the ordinary run of co-operatives for tax purposes?

MR. HALLINAN: I would say that is a correct statement, sir.

MR. STEWART: Now, when we come down to a comparison of credit unions, not only with co-operatives, but with the other types of financial institutions with which you appear to compete, or if you prefer, which are attempting to compete with you, why is it that you think that they should be taxed but you should not?

MR. HALLINAN: We have no opinion on their status. We maintain that any financial institution that operates in the manner of a credit union should be treated exactly like a credit union.

To go back to an earlier question of yours, Mr. Stewart, you suggested that an individual person now could invest money and get a similar return and almost get the same deal when it came to borrowing. I do not think that is quite true. I would like to amplify the remarks that Mr. Burton made.

Many of our larger credit unions are able to render their members a much more reasonable, cheaper service than they can borrow the money from any other financial institution. I am thinking of some of our larger credit unions that can pay a return of, say, 4 to 5 per cent and either reduce their interest rates three-quarters of one per cent or at the end of the year I have known of a credit union in the city who have given a rebate of 35%.

Now, that is an exception. It is not the general rule, but the trend is in that direction, which means that the net cost of that loan to that individual

member is considerably lower than he could get it from any other financial institution.

We are, therefore, doing that member a real service. We are increasing his purchasing power and generally assisting society.

MR. STEWART: Let me come back to Appendix 3, Mr. Hallinan. It relates to some 1,315 credit unions, and the amount of income shown is some $21,000,000. That is gross income. Then after expense, the amount of income shown, the amount of net income, is some $12,489,000. That would appear to work out on the average at just under $10,000 per credit union. If I divide $12,489,000 by 1,315 I think I get something just under $10,000. Do you agree with that?

MR. HALLINAN: That is right, sir.

MR. STEWART: Now, on that basis - and I realize that I am talking now about averages and that there will be some below average and there will be some above average if the average credit union in Ontario were taxed as an ordinary corporation under the Income Tax Act, it would be taxed at the low rate of corporate tax which applies to corporations with taxable income up to $35,000.

Now, my question is this: if that is the fact, and if the average credit union were subjected to a tax in Ontario of 23% on its income of $10,000, would that, in fact, have a serious adverse effect on the operations of that union?

MR. BURTON: Mr. Stewart, first of all, if, for instance, the Government decided to tax credit unions the same as other financial concerns in 1964, 1965, it is very

doubtful whether such profit figures or net earning figures as are shown in these statistics would appear because the majority of credit unions will presumably do what some are beginning to do already, and reduce their interest rates from 1% to three-quarters, which is one of the things they would do to cut down their net earnings.

MR. STEWART: Yes, but you are suggesting what they would do - I think the expression which is commonly used is "price out" in the case of co-operatives, at any rate? Would that, in fact, be necessary, Mr. Burton, when what you are talking about is 23% of $10,000 in the average case or a tax of $2,300 per annum?

MR. BURTON: Yes, because the credit union people feel that they are borrowing their own money, and this is true of the credit union movement. They put their money in and the same people borrow it. Some do not borrow, of course. Some save more than others, but they are borrowing one another's money, and therefore they would say, if it were to be taxed, we must, as near as possible, operate at cost. This is a very legitimate way of doing it, as one large credit union in the province that I know of has reduced the interest rate to three-quarters of one per cent. They do not pay any rebate, and automatically they are reducing their net earnings.

Then, if the credit union encourages deposits rather than shares on which a fixed interest is paid which is charged as an expense, this would further reduce the net profit and it would reduce this figure here of twelve-and-a-half million. It could quite reasonably be reduced two or three million, which would bring down your

average per credit union to about $2,500. Twenty-three per cent of $2,500 is pretty small, and of course they could not possibly object to that.

Therefore, to go back to your other question, we would not feel it would have an adverse effect on the credit union movement.

MR. STEWART: When you say it would not have an adverse effect on the credit union movement is that because the method of operating would be altered?

MR. BURTON: Because the method of operating would tend to be as near cost as possible because the intention of the credit union when it goes into operation is not to make a profit. It only goes into operation to serve its members.

MR. STEWART: That is, of course, the philosophy behind the movement, but is there not, Mr. Burton, a real question now having regard to the growth of the movement and having regard to the increased size of the average credit union, whether these credit unions are not in fact in business for profit?

MR. BURTON: We maintain that the question of size is irrelevant because the principle and philosophy is exactly the same. Because it has multiplied ten times in 20 years does not change the original intention. There may be the impression among very big credit unions that they are in business to make a profit, but it is the other way around. Profit is incidental to their growth. The bigger they get and the lower their costs, the higher their proportion of net earnings, but this picture would be altered if they attempted to operate at cost, and the

credit union which could most successfully do this would be the large one because of their practices of budget making and because they know so well how they did last year and they can anticipate what they are going to do next year. They are very stable, so we maintain any business for profit is an illusion, just because they happen to make a large surplus, the bulk of which comes back to the members.

MR. STEWART: Now, Mr. Chairman, the hour has moved on and this is a matter which we could obviously discuss at some length but I think I had better desist at this stage and close my examination.

THE CHAIRMAN: All right, Mr. Stewart, thank you. I think there will be a few questions up here. Just continuing with the last point, I do not think I know the distribution between dividends and rebates. They are set forth in a total amount of $8,926,000 on Appendix 3. It just occurs to me if I take 4% of the total amount of shares outstanding I would get over seven million dollars, which does not leave an awful lot for interest rebates. Is there a distribution between the two figures?

MR. HALLINAN: Unfortunately we have not a breakdown between dividends and rebates, Mr. Chairman. These statistics were provided by the Government of Ontario, and they did not give a breakdown.

THE CHAIRMAN: Would you have that broken down in your own figures which do not exactly match these?

MR. BURTON: No, we do not have them here, Mr. Chairman. I could give you a very rough guide. I think

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you will find that the dividends probably amount to just

over two-thirds of that figure. This is based on the average rebate of 16%, and the interest rebates would account for just under a third.

THE CHAIRMAN: Thank you.

COMMISSIONER GRANT: I would like to refer to the method of acquiring shares, and would you please explain how shares are allotted?

MR. HALLINAN: First of all, we in the credit union movement would like to refer to shares as units of savings. In other words, the credit union movement is built up trying to get people to acquire the habit of thrift, and the only way they can do that is by making regular deposits in the credit union usually every pay day or weekly or bi-monthly or monthly. As each five-dollar unit comes in, the member has acquired a new share.

As has been pointed out earlier, sir, there are no share certificates issued. The receipt of the share is evidenced by a pass book. The shares do not fluctuate in value. They remain constant, usually at $5 - not more than $10 in this province - and the individual builds up a savings account in his credit union by regularly depositing in his share or deposit account. It is a continuing process - we hope and try to encourage it to be a continuing process.

COMMISSIONER GRANT: The borrower does not receive any shares?

MR. HALLINAN: He is encouraged to continue saving whilst he is repaying his loan.

COMMISSIONER GRANT: So the borrower ---

MR. HALLINAN: He is a member as well as the

saver.

COMMISSIONER GRANT: The borrower has a deposit account with you as well as the loan account?

MR. HALLINAN: Yes. In other words, before a person can borrow he must become a member. To become a member he must pay an entrance fee of, usually, 25 cents, and make a subscription for at least one share and then he becomes eligible to borrow.

COMMISSIONER GRANT: On your balance sheet your personal loans about equal your shares?

MR. HALLINAN: That is correct.

COMMISSIONER GRANT: In addition you have mortgage loans totalling $34,000,000 at the end of 1961. Those mortgage loans are made by the union without any supervision from the central organization?

MR. HALLINAN: Well, I would not say without any supervision. The Department of Insurance has laid down certain rules and regulations that a credit union must follow before it can get into the mortgage field. In other words, it may not at any time have more than 25% of its assets invested in mortgages. They may lend up to 60% of the appraised value of the house, and the loan is secured by a first mortgage on real estate.

COMMISSIONER GRANT: Are your mortgage loans, on a percentage basis, increasing quite rapidly?

MR. HALLINAN: Speaking of this province only, sir, I would say there is no great increase in the mortgage field. It is a very slow but gradual increase. Nothing spectacular.

COMMISSIONER GRANT: In your investment account

on the assets side of your ledger, you show a total of $26,000,000 which would consist of your guarantee fund, your undivided earnings, your other funds and reserves. Am I right so far?

MR. HALLINAN: May I ask Mr. Creswell, who has statistics on that, to answer that question?

MR. CRESWELL: Mr. Chairman, these guarantee funds are not, in the Province of Ontario, required to be invested by law, nor are the undivided earnings. However, I venture to say possibly your statement is correct in that the surplus funds on hand must go some place and they have probably gone in the bank. Our investments are ones that fluctuate all the time because our attempt is to loan out of our funds to our members. Therefore, as a result, we find that only 3.3% of our total assets are invested in long-term investments which usually are government bonds or government guarantee bonds.

The remaining 5.8% of this amount is in the hands of our League Central, and other Centrals, perhaps, throughout Canada hold these funds so that they can loan it out to other credit unions that are in need of funds.

COMMISSIONER GRANT: You would think about $7,000,000, probably, in the investment account would be in government bonds?

MR. CRESWELL: That would be correct.

COMMISSIONER GRANT: Your investment account also, then, includes loans to members?

MR. CRESWELL: No, the investments would not include loans to members. The credit union would invest its funds with our League, for example.

COMMISSIONER GRANT: I understand.

/MC/ss

THE CHAIRMAN: In reply to Mr. Grant I think you stated in order to secure a loan a borrower must become a member and that required 25¢ payment on a subscription to one share of capital stock which was $5.00. Is that correct?

MR. HALLINAN: Not exactly, sir. A person, to become a member of a credit union, pays an entrance fee of 25 cents and then he must subscribe for at least one share and make a down payment on that share.

THE CHAIRMAN: What is the down payment?

MR. HALLINAN: It could not be less than 25 cents. In all practical cases they usually buy a share outright.

THE CHAIRMAN: So in order to become a member he pays an entrance fee of 25 cents and makes a down payment on a $5.00 share and the down payment is not generally less than 25 cents.

MR. HALLINAN: That is correct.

THE CHAIRMAN: We don't have your statement on the Ontario Organization, Ontario Credit Union League Limited.

MR. HALLINAN: We have it in the annual report.

MR. BURTON: We have six copies here.

THE CHAIRMAN: They are not with us here, I am afraid. We would like to see them.

THE SECRETARY: I would like to enter one of these into the record as an exhibit, Mr. Chairman.

MR. STEWART: Could we at the same time enter as an exhibit this pamphlet which Mr. Hallinan has identified, the Credit Union Yearbook for 1962.

THE SECRETARY: Exhibit No. 74 and Exhibit 75.

MR. STEWART: Which is which?

THE SECRETARY: 74 will be the Credit Union Yearbook.

MR. BURTON: Could we use that one until the questioning is finished?

THE CHAIRMAN: Yes.

---EXHIBIT NO. 74: Credit Union Yearbook for 1962.

---EXHIBIT NO. 75: Annual Report of the Ontario Credit Union League Limited.

COMMISSIONER BEAUVAIS: I have a couple of questions to ask. The brief says that the credit union does not exist to compete with other organizations, and on a question by Mr. Stewart you said that there other banking institutions are competing with you, because they were formed or they entered into that kind of business after you had entered. Is it not true, however, that in the Province of Quebec there are two savings banks that were long established before the credit union, namely, the Quebec Savings Bank, 110 years, and the Montreal City and District Savings Bank.

MR. HALLINAN: That could quite possibly be true, Mr. Chairman. Unfortunately I am not as familiar with the scene outside of Ontario as I would like to be.

COMMISSIONER BEAUVAIS: Nevertheless, in Quebec they might compete with two Quebec savings banks.

MR. HALLINAN: That is a possibility.

COMMISSIONER BEAUVAIS: Thank you. Another point, I am coming back to the rate of interest, 1% per month. You said that the average rate was about 5½%, I think. The effective rate per annum remains at 12%?

MR. HALLINAN: 12% simple interest is effective.

COMMISSIONER BEAUVAIS: That is all.

COMMISSIONER WALLS: You mentioned the fact that the banks are now granting loans on six tests. To what extent do you govern the loaning to new applicants? Is it necessary today for you to require an endorser in granting a loan to somebody you have no previous contact with?

MR. HALLINAN: Not necessarily, Mr. Chairman. The regulations regarding loans are generally set forth in the credit union bylaw. The credit union may loan up to $200.00 unsecured and from $200.00 to $3,000.00 on security. The security that is frequently given is a wage assignment or a chattel mortgage. If a member comes in to borrow $2,000.00 to purchase an automobile, the credit union will take a chattel mortgage on that loan.

The big thing that guides the Credit Committee in granting a loan is the character of the individual person. That bears out once again the tremendous advantage of having a credit union work within a common bond of association. You work with this person that has applied for the loan, you go to the same church, live in the same well-defined community, a member of the same fraternal organization. You know the person.

The most important thing in guiding a Credit

Committee in dealing with a loan application is the person's character, his ability to repay. The loan must be to a provident and productive person. Sometimes you are doing a favour by refusing a loan if in the wisdom of the members of the Credit Committee we would be doing that man a disservice if he borrowed beyond his means to repay or for some foolish purpose.

COMMISSIONER WALLS: You still operate on the same basis as the bank insofar as if an applicant is doubtful and he can get an endorser whose credit standing is good, then you will grant a loan based on endorsation of a note.

MR. HALLINAN: We can do it that way. We also must take into account the point of view of justice to the person endorsing. If a person is a known deadbeat and he came and said he could get a reputable person to endorse the loan, we would not necessarily grant the loan. We would surmise that the actual borrower was not worthy of the note and if the loan did become delinquent the co-signer would be held responsible and that would be for him disservice.

COMMISSIONER WALLS: Can all of your depositors withdraw their money at any time?

MR. HALLINAN: Yes. The credit union may require 30 days' notice to withdraw deposits or 60 days' notice to withdraw shares. However, in practice it is very rarely the fact. For all practical purposes he can come into the credit union office and withdraw.

COMMISSIONER PERRY: I have three or four questions which are closely related. First of all, could

you explain the basis of the emphasis on shares in the credit union movement? I notice someplace in your brief you say share ownership has always been regarded as the fundamental source of capital. Is there some philosophy behind this?

MR. HALLINAN: Yes, there is. The philosophy is this: The credit unions are primarily set out to encourage people to acquire the habit of thrift. The best way they can do that is making regular deposits in the share account in the credit union. We like a person to think of creating a measure of economic security. We encourage him to leave it in and not withdraw it. If he is in need of funds for a short term we recommend he leave his savings in and borrow the money.

COMMISSIONER PERRY: The fact being there is something more tangible about having a share account than simply having a deposit, I suppose.

MR. HALLINAN: That is quite correct.

COMMISSIONER PERRY: Another question is whether you have any views as to the possible ultimate growth of the credit union movement in Ontario.

MR. HALLINAN: Well, of course the credit union movement by their very nature is dynamic. The ideal situation would be if every man, woman, and child in this great country were a credit union member. That ideal, of course, will never be reached. As the economy of the country develops,new industries come into being. We always encourage the formation of a credit union wherever it is warranted.

COMMISSIONER PERRY: Would you think if eventually

the whole financial system were operated by credit unions there would be still authority in your argument you should not pay income tax?

MR. HALLINAN: I would think so.

THE CHAIRMAN: What is that?

COMMISSIONER PERRY: He would think so. Several places in your brief you mentioned, and I don't doubt it at all, that taxes paid both on dividends and rebates of interest. Just what is the machinery by which you report these financial transactions both to your members and to the Income Tax Department?

MR. HALLINAN: Every credit union annually submits the usual returns to the Income Tax Department the same as any other corporation that pays dividends.

COMMISSIONER PERRY: What about the rebates of interest on borrowing?

MR. HALLINAN: Of course that is only true in the case of a business loan where the businessman has borrowed money and has used the interest that he has paid as a legitimate expense. If it is in the case of an individual person it means he has borrowed that money at a lower cost than it would appear.

COMMISSIONER PERRY: What is the actual machinery by which you bring about this result? Is it a credit against the outstanding loan?

MR. HALLINAN: Usually the dividends are credited to the member's share.

COMMISSIONER PERRY: I am sorry, I mean the rebate of interest.

MR. HALLINAN: The same way.

COMMISSIONER PERRY: It is made as a credit?

MR . HALLINAN: Yes.

COMMISSIONER PERRY: Would you give us some idea of what are the trends of growth within the various types of Credit Unions? I see that in Ontario industrial unions are the largest single group. Is this where the growth is now taking place?

MR. HALLINAN: Yes, in this province it is chiefly in the industrial field.

COMMISSIONER PERRY: Could you just for our own information mention a few of these industrial unions which are now quite large.

MR. HALLINAN: The largest industrial credit union in Canada is 10,000 employees of the Steel Company of Canada in Hamilton. They have two or three credit unions in the province, Stelco they call them. We have many larger credit unions. For example, the Hydroelectric, Bell Telephone, Ontario Municipal Employees, we have many credit unions in the civil service, both Federal, Provincial and municipal. In the automobile industry, there is the Autoworkers in Oshawa at the General Motors.

COMMISSIONER PERRY: What would be a large industrial credit union in Toronto, for example?

MR. HALLINAN: Hepco.

COMMISSIONER PERRY: The Hydro?

MR. HALLINAN: Yes. They have assets of about twelve million.

THE CHAIRMAN: Roughly how many members would they have?

MR. HALLINAN: They have about 12,000 members at

Hepco.

THE CHAIRMAN: I thought you indicated a limit was placed by Statute of 6,000.

MR. HALLINAN: That is for community types.

COMMISSIONER PERRY: What is a common community type of union? Could it be such a thing as all the persons in one town?

MR. HALLINAN: Take the Town of Clinton, Ontario. They have a closely-knit credit union there. There is also Dundalk. It is another type of community union that serves the people in the Dundalk area.

COMMISSIONER PERRY: Could you conceive of a community type union in Metropolitan Toronto?

MR. HALLINAN: No, that is out as far as the Department goes.

COMMISSIONER PERRY: Because of the 6,000 membership?

MR. HALLINAN: Yes. It has a potential of 6,000. As long as the population is more than 6,000 the Department will not grant a charter.

COMMISSIONER PERRY: Then you mention that some credit unions took deposits mainly as a facility for checking. Is this sort of thing on the increase, or what is likely to happen?

MR. HALLINAN: I would say not appreciably so. At the present time only 6% of the credit unions are using it and of those 6%, it is only a small percentage of the members, according to our records, that are taking advantage of this secondary checking service.

COMMISSIONER PERRY: These instruments are

issuable to third parties like any ordinary bank cheque.

MR. HALLINAN: That is true.

COMMISSIONER PERRY: Are there credit unions which engage in active programs of advertising in the public press or radio?

MR. HALLINAN: Yes, there are some, although advertising in the public press is not too effective, because before a person could become a member they must share an original common bond. In Oshawa the Autoworkers' Credit Union membership is limited to employees of the General Motors Corporation. If they put an ad in the local press they could conceivably have hundreds of people replying to the advertisement who would not be eligible for membership, not employed by General Motors. Take a church credit union. If they put an ad in the paper, unless the person was a member of that parish or congregation, they would uneligible for membership.

COMMISSIONER PERRY: I seem to remember seeing advertisements that did appear in the press, but these would be in the terms that they were drawing to the attention publicly of eligible members the services of the credit union.

MR. HALLINAN: That could be.

COMMISSIONER PERRY: That is all, I think, Mr. Chairman.

THE CHAIRMAN: Continuing that thought about public relations, I observe that the Ontario League spends about $176,000.00 on public relations which, I think, is probably pretty largely spent on your news, which has a circulation of 100,000 a month. I expect it is also

expended on T.V. and press. Would that be right?

MR. HALLINAN: No, I am afraid we spend very little on the T.V. or press. We put on a contest, to draw attention to the credit union, a selection of Miss Ontario Credit Union. We spend a few dollars there.

THE CHAIRMAN: Most of that sum would be spent on the magazine, would it?

MR. HALLINAN: That is true, yes.

COMMISSIONER MILNE: I have just one question to ask of Mr. Hallinan, and it deals with family financial counselling. It is not an involved question at all. I was interested in that point and wondering really if the type of counselling that is given here is by trained personnel, if this is a place where Honoraria would be required and to what extent this counselling is given.

MR. HALLINAN: The financial counselling is a relatively new development in this League. The textbooks prepared are prepared by experts in that field. We have adopted, through our own Educational Department, to put it on a Chapter level, that is a group of credit unions, say, in the City of Toronto or Hamilton. To illustrate the point, last week the second of two family counselling classes was put on. The first one was for the ladies where they had experts who explained the proper way to purchase clothing, how to get value for it. The one prior was put on by the meatpacking plants showing to the wives particularly the best method of purchasing meat, where you get the most value for your dollar. Then it goes on to further counselling in the method of purchasing

automobiles, family budgeting, which is a very important thing. It is that type of thing we are moving.

COMMISSIONER MILNE: Then the cost as such would come out of the education dollar.

MR. HALLINAN: That is correct.

COMMISSIONER GRANT: I just have one question that I would like to ask you, and that comes back to the question which I previously asked with respect to the money which you raised by way of the balance sheet item of shares, which is made up of dividends and according to paragraph 72 on page 29, it also includes interest rebates.

Now, when you decide on the percentage of your net profits that you are going to return to your borrowers by way of interest rebates, I understand from your brief that that is credited to the shareholder's account, not to his borrowing account, to his share account.

MR. HALLINAN: Generally speaking, that is so.

COMMISSIONER GRANT: Now, he is taxable on his dividends, but he would not be taxable on his interest rebates; would he?

MR. HALLINAN: No, he would not be.

COMMISSIONER GRANT: So do you advise him, do you advise each of your shareholders, so-called, of the amount of dividend that has been credited to his account and the amount of interest rebate that has been credited?

MR. BURTON: Yes, Mr. Grant. Many of the larger unions have dispensed with the passbooks and issue quarterly statements and after the annual meeting where the dividend and rebate are approved, the accounts are credited

individually with dividend and rebate which is clearly marked. They are not lumped together and put as one sum. For sums in excess of $100.00 the usual T-5 return is made by the credit union to the Government.

COMMISSIONER GRANT: If that member is paying income tax then he is bound to report the amount of the dividend?

MR. BURTON: That is correct.

COMMISSIONER GRANT: And he is paying tax on that dividend notwithstanding he leaves the dividend with you?

MR. BURTON: That is correct.

COMMISSIONER GRANT: And I would say from what I have heard that there is relatively little withdrawal of dividends, or small.

MR. BURTON: I think that is generally true.

COMMISSIONER GRANT: And yet your degree of liquidity depends upon what I should think would be a rather precarious method of raising money in that it can be withdrawn. The man is paying tax on it and he can withdraw it and yet by far the greatest amount of your loans are made from this source of money.

MR. BURTON: If in an individual credit union there was for some reason a run on the bank, so to speak, it would have to be made clear to the members it would be difficult for a large proportion of them to withdraw their money if at the same time it was on loan to their fellow credit union members.

COMMISSIONER GRANT: You have a provision whereby you can require 60 days' notice.

MR. HALLINAN: There is another safeguard, if I might interject. If an individual credit union is experiencing an excessive share withdrawal they may apply to the League for a loan from us and added to that is a further safety valve known as our stabilization fund which has just been in operation for two years. The purpose of it is to stabilize any credit union that finds itself in an awkward position.

THE CHARIMAN: Mr. Grant, perhaps to round out your question, I will ask him if any credit unions have failed in recent years in Ontario.

MR. HALLINAN: Some have liquidated due to the basic bond of association disappearing, but certainly in recent years every credit union that has surrendered its charter has paid off 100 cents on the dollar.

MR. STEWART: I think the record s hould perhaps be clarified in one respect. Mr. Walls and I were talking about Service Co-operatives. We got onto that subject because I had suggested to these witnesses that perhaps credit unions were in the position of service co-operatives and we were discussing both the taxability, the possible taxability of a credit union or service co-operative itself and the member in relation to dividends or patronage dividends.

Mr. Walls has reminded me under Subsection 6 of Section 75 of the Income Tax Act the member of a co-operative is not taxable in respect of patronage dividends relating to consumer needs or services. I thought I should put that on the record, because as far as the member of a Service Co-operative is concerned his

patronage dividend might not be taxable in his hands.

THE CHAIRMAN: Thank you, Mr. Stewart. Does anybody have any further questions? Mr. Stewart, have you anything?

MR. STEWART: Nothing further, sir.

THE CHAIRMAN: I think that completes our questions. Gentlemen, have you anything more you would like to say to us?

MR. HALLINAN: No, Mr. Chairman, thank you.

THE CHAIRMAN: We are very grateful to you indeed. You put forward an excellent submission. We will continue to review this matter, I can assure you. We indeed thank you very much for your attendance and assistance. Good
4 day, sir.

MR. HALLINAN: Thank you, sir.

THE CHAIRMAN: Mr. Secretary, it being twelve o'clock, it would seem to me that we should stand over until this afternoon. Now, I know that we have arranged to see the next participants at eleven o'clock, but it would be quite unsatisfactory I would think, for an important submission to start now and go for fifteen or twenty minutes. Would you ask these gentlemen, if they are in the room, if it would be satisfactory to them to stand over until 2:15. Would that be satisfactory to you?

MR. GORMAN: Yes.

THE CHAIRMAN: We will stand over until 2:15.

---The Hearing was adjourned until 2:15 p.m.

THE CHAIRMAN: Mr. Secretary, would you put us in motion and introduce our visitors?

THE SECRETARY: Mr. Chairman, we have with us this afternoon Mr. John Gorman, President, and Mr. D. Rolling, Manager pro tem of the Retail Merchants' Association of Canada (Ontario) Incorporated. This body has presented a brief to the Royal Commission, and they are here to speak to it, and I would like to enter it into the records as Exhibit No. 76.

---EXHIBIT NO. 76: Brief of the Retail Merchants' Association of Canada (Ontario) Incorporated.

SUBMISSION OF

THE RETAIL MERCHANTS' ASSOCIATION OF CANADA (ONTARIO) INCORPORATED

APPEARANCES:

Mr. John Gorman	President
Mr. D. Rolling	General Manager Ontario Association

THE CHAIRMAN: Thank you, Mr. Secretary. Good afternoon, Mr. Gorman. Please forgive us for being late. I am sorry. We announced 2:15, but we did not make it, because we were entertained for lunch. Now, Mr. Gorman, you are with Mr. Rolling.

MR. GORMAN: Yes.

THE CHAIRMAN: If you would care to speak to your submission, we would be very glad to hear from you. We have questions to put to you. We have our legal adviser and counsel whom we have asked to lead the questioning

in order that we might do justice to this excellent work that you people have prepared. We have, I might say, found it most interesting, but before we commence with our questions, have you anything else that you would care to say to us?

MR. GORMAN: Thank you, Mr. Carter. Very briefly, yes. My name is John Gorman, from Saulte St. Marie, Ontario. I am a small businessman and I am active in the operation of four Ladies' ready-to-wear stores, Saulte St. Marie, Port Arthur and Fort William, in the Province of Ontario. I am also President of the Retail Merchants' Association of Canada (Ontario) Incorporated, and in this context it is my pleasure to be appearing as the official representative of that Association.

I would like to introduce Mr. Rolling, Mr. D. W. Rolling, General Manager of our Ontario Association, who will be available for any questions that you may wish to direct to him. I will be very brief.

If I may, I would like to summarize very briefly our thoughts and make our recommendations. It is the purpose of this submission to direct the attention of the Commission to the fact that our present income tax legislation is inequitable and confers tremendous tax concessions on cooperative associations to the detriment of their fully-taxed competitors.

This is a matter of grave concern to the retailers of this country owing to the unfair competitive advantage granted by our tax laws to the cooperative trading organizations which are highly concentrated in the distributive marketing and service sectors of the

economy.

We are also firm in our opinion that this inequitable situation is uneconomic in its relationship to the national welfare. It involves misallocation of the nation's resources, loss of revenue to the Federal treasury and shifts the tax burden to the shoulders of other taxpayers.

Cooperatives are flourishing and expanding in their realm of activities at rates of growth which exceed national averages. Page 39, as I recall it, in our brief, indicates July 31, 1961 a 7.2% increase, which I would compare with the mere 1% rise in Canadian sales generally. Their outward signs of prosperity are fully backed up by real financial success.

No case has been made out to show that cooperatives are a superior form of business or more efficient than other businesses. Alternately, there is conclusive evidence we feel to show that the extraordinary growth of cooperatives is due not to their efficiency, but to the financial advantages which are accruing to them under the present tax arrangements.

We would clearly establish and I feel that we have in our brief that cooperatives have personalities distinct from those of their members, that they are organized for the gain of their members, that they earn income and allocate their profits to their own patrons. The return to any one member is not simply a repayment of the overcharge made to that particular member; it represents the result of and the profit on all the cooperative trading ventures.

The cooperative member, just like an investor in an ordinary company, participates in the trading fortunes of his cooperative. We suggest that there are valid reasons for requiring cooperative organizations and their members to shoulder their share of the tax load, and we add that our request for tax equality does not imply disapproval of the cooperative idea. The businesses we represent are rather used to taking on competition of any kind. All we ask is that the ground rules be the same.

In consideration of the relevant importance of the corporate taxation contributions to the Federal treasury, it is the view of the Retail Merchants' Association that the only practical solution to the cooperative ordinary business tax controversy is tax legislation amended to impose a fair rate of tax on cooperative profits.

Now, we have three recommendations. Firstly, the repeal of Section 73, Subsection 1 of the Income Tax Act to remove the discriminatory three-year exemption for new cooperatives. Secondly, the amendment of Section 75 to disallow the deduction of patronage dividends in the calculation of net income of either cooperatives or ordinary corporations; thirdly, provisions for tax treatment of patronage dividends in the hands of recipients similar to that imposed on corporation dividends in the hands of shareholders, granted at the same time equal tax credits or allowances which may prevail. We believe these recommendations to be consistent with the principles of justice and equality. They offer a solution

to the cooperative taxation problem, and would have the effect of placing cooperatives and their members on an equal footing with proprietary businesses and their stockholders.

Thank you very kindly for you attention.

THE CHAIRMAN: Thank you, Mr. Gorman. Mr. Stewart, would you care to lead off?

MR. STEWART: Thank you, Mr. Chairman. Mr. Gorman, looking at page 2 of your brief, paragraph number 1 on that page, I take it that the Association which you represent is a provincial association of Ontario retailers, and that it is affiliated with a number of similar provincial retailers and with a Dominion association which is called the Retail Merchants' Association of Canada Incorporated.

MR. GORMAN: Yes, sir.

MR. STEWART: Would you tell us how long you have been connected with the Ontario Association?

MR. GORMAN: I have been connected in an executive capacity on the executive or directorate of the Association for a short four or five years.

MR. STEWART: Have you been a member for a longer period?

MR. GORMAN: I was a member two years prior to that.

MR. STEWART: How many members would there be in the Ontario Association?

MR. GORMAN: Well, at the present time our records indicate fully paid up membership of approximately 3,000.

MR. STEWART: On page 5 of the brief you indicate that as of 1961, there were about 60,000 retail stores in Ontario.Does that mean that there was something close to 60,000 retailers in the Province?

MR. GORMAN: Yes, I would say it would, sir.

MR. STEWART: I am just trying to determine whether your membership is 5% or 10% of the total number of retailers.

MR. GORMAN: Perhaps I was somewhat misleading when I quoted you 3,000 paid up members. It is a voluntary organization, and retailers use the services of R.M.A., and they are not always regular contributors. On a turn-over basis during the last five years, it is estimated that the aggregate membership was between 12,000 and 15,000 retailers. Many of these merchants do not regularly contribute, but because they have contributed once they feel they are bona fide Retail Merchants' Association members and identify themselves with membership in the Retail Merchants' Association.

MR. STEWART: Let me understand then more clearly. You mention a figure of 12,000. Is that an average figure or is that the total over that period of years?

MR. GORMAN: On a turn-over basis during the last five years we had an aggregate membership of between 12,000 and 15,000 retailers. At the present time we have 3,000 dues-paid members.

MR. STEWART: Well, when you say on a turn-over basis you had 12,000 to 15,000 in the aggregate, over a period of five years, that would seem to indicate that

3,000 at one time would be more or less an average.

MR. GORMAN: I would say that would be an accurate figure.

MR. STEWART: Is a chain store eligible for membership in your Association?

MR. GORMAN: An individual store by and large --- individual stores make up the bulk of our membership. Large corporate chains may appoint a member as a representative.

MR. STEWART: Do they in fact do that?

MR. GORMAN: Small corporate chains --- small chains. Not large groups.

MR. STEWART: I take it you regard your Association as essentially an Association of the smaller retailers.

MR. GORMAN: Yes.

THE CHAIRMAN: I am confused over the figures. I have three different figures. 3,000, 12,000 to 15,000 and 60,000.

MR. STEWART: Well, Mr. Chairman, 60,000 is the figure that appears on page 5, paragraph 3. There are 60,000 retailers. As I understand what Mr. Gorman is saying, over the period of the last five years they have had 12,000 to 15,000 in the aggregate over that period paying dues or otherwise associated with their Association. At the moment there are 3,000, and he has agreed that that is perhaps an average figure, which, as I see it, would mean that they represent some 5% of the retailers at any one time.

MR. ROLLING: Could I clarify that just a little more?

MR. STEWART: Please.

MR. ROLLING: We have many members, who, although they do not contribute on an annual basis, do regard themselves as once a member of the Retail Merchants' Association, always a member of the Retail Merchants' Association, and many others, who are Retail Merchants' Associations of local groups and regard us as their guiding star or someone who assists them when it is required.

In evidence of this here are seven copies of a report from the Cornwall Standard Freeholder of May 13, in which the local Retail Merchants' Association --- if I could offer those, sir --- regard themselves as part of the Retail Merchants' Association.

I offer too, further evidence of that. Here is another organization from Brampton, Ontario, who work as the Retail Merchants' Association of Brampton, and this is their formation of a manifesto that they wish to accomplish with our help and guidance. I have additional copies of that too, sir.

MR. STEWART: The first of these documents you have handed me indicates that you are going to discuss new trends in retailing at a meeting open to the members of the Cornwall Merchants' Association and the East Cornwall Businessman's Association.

MR. ROLLING: Yes, about 130 in attendance there.

MR. STEWART: So that it would indicate that these local or municipal associations look to you for assistance.

MR. ROLLING: That is correct, sir.

MR. STEWART: For assistance and advice. Unless you wish it, I do not think it is necessary to enter this as an exhibit.

THE CHAIRMAN: No, I do not think so. I want to get the figures straight. There are 60,000 retail stores and 12,000 to 15,000 retailers which means that each retailer would have four to five stores.

MR. ROLLING: No.

THE CHAIRMAN: 60,000 retail stores and 12,000 to 15,000 retailers.

MR. STEWART: 12,000 to 15,000 are simply the number who have some identification with this Association over a period of time.

THE CHAIRMAN: That is the number of retail stores which has been connected with this Association?

MR. ROLLING: That is right.

THE CHAIRMAN: It is the number of retail stores or retailers?

MR. ROLLING: Retailers. We have also associate members that are confined within the Province of Ontario that could be distributors or manufacturers that pay an associate membership where they are dealing with the retailer, particularly in the Province of Ontario.

THE CHAIRMAN: Of these 12,000 to 15,000, 3,000 are now members; is that right?

MR. STEWART: Are now dues-paying members I take it.

MR. ROLLING: Active members.

THE CHAIRMAN: And on page 5 where it says there are 180,000 retail stores of which slightly more than

60,000 are located in the Province of Ontario, that could well mean that there are 180,000 retailers? The term retailer and retail stores are synonymous here?

MR. ROLLING: Right.

MR. STEWART: Are you saying that the terms retailer and retail store are synonymous or would the average retailer have a fraction over one retail store?

MR. ROLLING: No, I would think they would be synonymous on an average, yes.

THE CHAIRMAN: Mr. Gorman has three, I think he said?

MR. STEWART: Four.

THE CHAIRMAN: Do you rate four times in the 60,000 or once?

MR. GORMAN: I only rate once, sir.

MR. STEWART: Now, gentlemen, do you and your Association classify your members according to income groupings?

MR. ROLLING: No, we do not.

MR. STEWART: You have no information as to the incomes of the individual members of your Association?

MR. ROLLING: We do not enquire into it unless it is given to us in confidence in conversation, that is all.

MC/dpw

MR. STEWART: Well now, looking at page 6 of your brief, paragraph 6, at the top of the page, I observe that in 1960 10,819 retail companies had a net taxable income of 244.4 million dollars and contributed 86.8 million dollars in corporation tax.

Then you refer to Table IV which contains additional information on this particular question but if I divide that net taxable income of 244.4 million by 10,819, which is the number of companies, I think I find that the average net taxable income of the 10,819 would be something under $25,000 per annum.

MR. ROLLING: That is correct. The basis of that table is in our taxation statistics for 1962, page 94, and is repeated in its entirety there. Income distribution by occupational class.

MR. STEWART: If it is still the case that your average member has a taxable income of something in the area of $25,000 the average member is taxable only at the low rate of corporate income tax. Is that correct?

MR. ROLLING: Twenty-three per cent.

MR. STEWART: And, of course, you point out in Table IV that 244 million dollars does not take into account lost companies of which, in the 1960 taxation year, there were 5,420.

MR. ROLLING: That is correct.

MR. STEWART: Then I also note from page 6 of your brief that - I take it it is in the same year, the taxation year 1960 - there were 77,733 business proprietors in the retail trade who paid tax and that the total tax paid was 45.4 million dollars. I think you would agree

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that the average amount of tax paid by each of those business proprietors was substantially under a thousand dollars in that year.

MR. ROLLING: That is correct.

MR. STEWART: And, again, looking at Table V, it is plain that those 77,000-odd taxpayers are exclusive of another 40,000 taxpayers who, in that year, did not pay any tax at all.

MR. ROLLING: Right.

MR. STEWART: Is that correct?

MR. ROLLING: Right.

MR. STEWART: Now, on that basis, dealing with these individual retailers again in Table V, they had income aggregating $419,000,000 and their total tax was $45,000,000, so that I calculate that tax as being at an average effective rate of approximately 11%.

MR. ROLLING: Yes, approximately.

MR. STEWART: Now, gentlemen, I observe on page 8 of your brief, in numbered paragraph 2, you indicate that you do not oppose co-operatives or the co-operative idea and that same point is made at a later stage in your brief. I also observe that on page 28 in the third and fourth paragraphs on the page you say, in effect, this: that in your opinion the essential difference between an ordinary corporation and a co-operative is that the ordinary corporation distributes its profits to its shareholders in accordance with the amount of capital they have invested in the corporation, whereas the co-operative distributes its profits to its shareholders or members in accordance with the volume of business they do with the

3 co-operative.

When you are comparing these two forms of corporate organization do you attach no significance at all to the fact that the owners of the co-operative are also its customers and, as I understand it, the co-operatives say that their members have come together because of some identity of interest of a type quite different from that which might bring the shareholders of a commercial organization together?

MR. ROLLING: They would be slightly different but the customers of the marketing co-op, their interest would be diverse to that of the co-op even though they might be a shareholder, whereas the corporation is treated slightly differently in that they are not necessarily the customers of the corporation but shareholders therein.

MR. STEWART: When you used just now the expression "marketing co-op" let me be sure we are on common ground here; just exactly what do you mean by a marketing co-op?

MR. ROLLING: Well, a co-op that would be in business in the retail field in a variety of lines which customers are buying or members of the co-op are buying and customers.

MR. STEWART: In other words, you are thinking not of the type of co-op which markets agricultural products for its members?

MR. ROLLING: No, I am not.

MR. STEWART: I think your use of this expression "marketing co-op" is perhaps a little unusual. It is unusual in my experience.

4 MR. ROLLING: It is covered generally here on page 29 of the last paragraph.

MR. STEWART: There is the marketing co-operative (1) which sells produce which is produced by its members.

MR. ROLLING: That is right.

MR. STEWART: And the term "purchasing co-operative," I take it, is the opposite to that. It is a co-operative which supplies merchandise to its members.

MR. ROLLING: Right.

MR. STEWART: I think, then, perhaps, I misunderstood you the first time.

MR. ROLLING: I am sorry.

MR. STEWART: Now, you said, as I recall, that there was a diversity of interest between the marketing co-operative and its members.

MR. ROLLING: There would be.

MR. STEWART: Perhaps you would indicate what that is so we understand each other.

MR. ROLLING: Diversity of interest might be they could be members necessarily of the co-op but not necessarily the same type of business the co-op is in even though they are shareholders in the co-op.

MR. STEWART: Here, are you talking about co-operatives that sell merchandise to their members?

MR. ROLLING: They sell it to their members as well as many others.

MR. STEWART: Yes. You are thinking of one that sells to members rather than the one that sells for members?

MR. ROLLING: I am thinking of one that sells to

5 members rather than the one that sells for members, correct.

MR. STEWART: Well, now, on page 9, the third sentence of paragraph 1, that is numbered paragraph 1, that a co-operative corporation keeps most of its profits and expands on tax-free income. Now, I wonder if you would tell us exactly what you mean by those words "expands on tax-free income."?

MR. ROLLING: I think we can refer you there to page 15 of our brief which refers to Section 75.

MR. STEWART: That refers to patronage dividends and do I take it then what you have in mind is that a co-operative which is taxed ---

MR. ROLLING: Paragraph 2.

MR. STEWART: We are now at page 15, paragraph 2.

MR. ROLLING: Paragraph 2, co-operative partisans.

MR. STEWART: Your basic point relates to patronage dividends.

MR. ROLLING: Yes.

MR. STEWART: And is the point you wish to make that a co-operative is subject to a limited amount of taxation and that it pays the patronage dividends to its members; they may be taxable in the hands of the members but they are credited to the members' accounts and are, therefore, until they are withdrawn, available for working capital and similar purposes? Is that what you mean by expanding on tax-free income?

MR. ROLLING: Yes, I would think that you would be generally correct, sir.

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MR. STEWART: Then you also indicate, on page 9, Mr. Rolling - I refer to the paragraph beginning on the last line on the page, that the basic problem you are concerned with at the moment has been enunciated by the increase in corporate tax rates. I take it that it has also been enunciated because of the fact, as you indicated in the last complete paragraph on page 9, a greater proportion of corporations are no longer of an agency nature so that a greater proportion are of the type - let me put it this way: when a larger proportion was of an agency nature the present tax rules were introduced and those which were of an agency nature were, in fact, excluded from tax altogether.

MR. ROLLING: There were two agencies probably at that time, going back some time on that.

MR. STEWART: Now, on page 10, you suggest that under the present rules, and I refer now to the first complete paragraph on that page, you suggest that under the present rules co-operatives could restrict their liability to as low as 5% of their profits. Now, could you indicate to us just how you arrived at that figure?

MR. ROLLING: That is the Federated Co-Operatives Limited for the year 1961 and the Alberta Wheat Pool have restricted their tax liability in the same manner.

MR. STEWART: Those, I take it, are very large co-operatives?

MR. ROLLING: That is correct. They are still taken as a good example of a continuing period of 5%.

MR. STEWART: If you take your average co-operative which has a comparatively modest amount of income I

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take it the 5% figure would not be borne out.

MR. ROLLING: I would think that most co-operative spokesmen would agree their trading transactions take place at current price levels and on the total volume last year of 1.5 billion it would appear to be fairly obvious they had a substantial amount, not necessarily all concentrated in the two I gave as an example previously.

MR. STEWART: Well, yes, I am quite certain they had a very substantial volume but could you give us examples of small co-operatives which can restrict their liability for tax to this 5%?

MR. GORMAN: I think it would be pretty difficult, sir, to get that information.

MR. STEWART: In any event, as far as this brief is concerned, you rely on the larger co-operatives?

MR. ROLLING: As a fairly good statement, yes. They are public figures. The Alberta Wheat Pool discloses a statement of 5% to be factual. Our brief submits also that the Federated Co-Operatives has managed to reduce its tax liability to 5% or less.

MR. STEWART: Then in that same paragraph on page 10, where you indicate that a co-operative is a vehicle for re-investment of tax-free income, are you referring there to the same point we have already discussed, that is that co-operatives are, in fact, or in practice, able to take advantage of patronage dividends for working capital?

MR. ROLLING: The point you brought up earlier, that is correct.

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MR. STEWART: Now, on page 13, you deal, with numbered paragraph 1, with what you describe as the three-year tax holiday and you ask that that be eliminated. I take it that you prefer such elimination to the granting of a similar tax holiday to all business.

MR. ROLLING: Well, it should be proportionate, sir.

MR. STEWART: I just assume, perhaps, you felt it would not be realistic to suggest every new business be granted a three-year tax holiday.

MR. ROLLING: We would agree with that statement.

MR. STEWART: Now, on page 14, in the second complete paragraph, you refer to the exemption from patronage dividends which is granted under sub-section 6 of Section 75 and which, as I see the section, is granted in respect of consumer goods or services.

Then, you go on, on page 14, to say that other patronage dividends, whether or not paid in cash, are taxable if the customer is in a tax-paying bracket.

BL/dpw

MR. ROLLING: Right.

MR. STEWART: But as I read your brief, you are objecting to the tax treatment of patronage dividends as a whole or, rather, to the tax treatment of co-operatives as a whole, and that your basic submission is that co-operatives should be taxed in the same way as an ordinary commercial corporation.

MR. ROLLING: We would suggest that.

MR. STEWART: Now, you deal, in fact, with the taxation of corporate profits at page 17 of your brief, and you indicate there that you doubt that the corporate income tax can be eliminated, but I noticed, at an earlier stage of the brief - and I am referring now to page 8 - that you say, I think, that the corporate tax should be reduced. There is a statement on page 8, on the first line of that page.

MR. ROLLING: If they were on the same basis, I think reduction of the corporate taxation would be automatic in that event, if the taxation load was shared by all.

MR. STEWART: I am talking, at the moment, only of corporate taxation. You are not advocating, at the moment, that corporate income tax be eliminated, but you are advocating that it be reduced; is that correct?

MR. ROLLING: Right.

MR. STEWART: Then, on page 20, gentlemen, in the third paragraph, you say that as matters now stand "the contribution of the individual corporation and its shareholders is several times as great as that of the co-operative group."

I would like to explore that with you a little bit having regard to what we have already found about members of your association, and at the moment I would like to deal with the average member of your association, realizing, of course, that there are some members whose incomes will be above average, just as there will be some whose incomes will be below average. But let's take the average member who we found earlier has an income, a taxable income, of approximately $25,000 per year. Now, at the present time, I think you would agree that he is subject - we are talking now about corporations - that that corporation will be subject to 23% corporate income tax, taking into account the basic tax, the old-age security and the provincial tax in Ontario.

We are agreed upon the 23% rate?

MR. ROLLING: Right.

MR. STEWART: If that corporation pays that rate and then chooses to distribute the balance of its holdings to its shareholders, I think you would also agree that under Section 38 those shareholders are entitled to a 20% dividend tax credit.

MR. ROLLING: Right.

MR. STEWART: And I, therefore, suggest to you that there is, on that basis, double taxation of corporate income in the case of the average member that we are talking about.

MR. ROLLING: Right.

MR. STEWART: Only to the extent of 3% of income.

MR. GORMAN: I am not quite as fast on figures as you are, sir, nor am I aware - I can't help but feel

that if that were so the co-operatives would have no hesitation in sharing the same tax advantages as corporations.

MR. STEWART: This is what I want to explore with you. I would like to make it quite plain that I am in no sense trying to trap you into any admission here. I think my mathematics are probably correct, that if the Government, when it taxes the smaller corporation at 23%, leaves the taxpayer with 77%, the taxpayer then proceeds to distribute that amount by way of dividends to its shareholders and then receives on those dividends a 20% dividend tax credit under Section 38.

MR. ROLLING: Right.

MR. STEWART: The double taxation element so far as the corporate income tax is concerned is arrived at by deducting 20%, that is 20 percentage points from 23 percentage points and it becomes 3%.

MR. GORMAN: It sounds correct.

MR. STEWART: Let us assume, without asking you to commit yourself, that that is so for the moment.

I would now like to deal with the case of the co-operatives.

THE CHAIRMAN: Mr. Stewart, may I interrupt for one second for the better understanding of the Commission?

MR. STEWART: Yes.

THE CHAIRMAN: It is $25,000 average; it is including, I would assume, large merchants, chain stores, and so on; Eaton's, Simpson's, Loblaw's, and whatever there may be. If that is the case, there would be a lot of incomes taxed at 50%, quite a lot taxed at the low rate.

MR. STEWART: Yes, Mr. Chairman. I am taking my figures from Table IV, as you will recall, and these are the figures which were referred to at an earlier stage of the brief on page 6.

I have pointed out that on page 6 it is stated that there were 10,819 retail companies with net taxable income of 244.4 million dollars, and the witnesses have gone along with me that on average this works out at something less than $25,000 per retail company, and I have been careful, I think, to emphasize that I am well aware that there will be many whose incomes are above that and who are therefore taxed at a higher rate. But I have simply suggested, as far as the average is concerned - and I admit that I suggested this would apply to the average member of this association - we are concerned simply with the low rate of corporate income tax.

If you take the large ones out, if you take out the chains, for example, the average of the balance would obviously go down substantially below what it otherwise is.

THE CHAIRMAN: Thank you.

MR. STEWART: Now, let us consider, gentlemen, the case of the co-operative, and I am thinking now of the co-operative which is taxable under the present provisions of the Act and the patronage dividends of which are also taxable.

Now, if I look at the section of the Act which relates to personal tax rates I find that if a person's taxable income exceeds $4,000 in the year - I am referring to Section 32 - if his taxable income exceeds $4,000, then the tax he pays on the excess is at the rate of 22%.

Now, that, of course, is an incremental rate, it is not an effective rate. But dealing with the incremental rate of 22%, would it not follow that the member of a co-operative who is taxable on patronage dividends may very well, at any rate, be taxed on an incremental basis at more than 20%?

MR. ROLLING: Would you repeat that last part of that again, please?

MR. STEWART: Surely. Let me give you a little more of what is in my mind, Mr. Rolling, because really what I am trying to find out for my own edification, apart altogether from that of the Commission, is whether you have something here you really should be concerned about. If we are thinking of the small retailer whose income is not more than $25,000 - and I am assuming that his business is incorporated - I am suggesting to you that in Ontario his basic rate of corporate income tax is 23% and he can get a 20% tax credit in respect of that. So that if all the earnings of the small corporation are distributed to its shareholders each year, which can be done, then they are taxed at their personal rates of tax plus 3%.

Now, when we come to the co-operatives which pay patronage dividends, to the extent that their earnings are distributed in patronage dividends or credited to the members' accounts by way of patronage dividends, I am suggesting to you that tax is paid by the member, and while obviously something turns here on the proportion of their earnings which is paid out by way of patronage dividends, I am suggesting this to you, that to the extent

2 that the earnings are paid out they are taxable at the personal rates of the shareholders; and if you assume that the average shareholder of a co-operative has some other income, then if his taxable income amounts to $4,000 and you take the incremental rate above that as far as the patronage dividend is concerned, he has paid tax of 22% under Section 32.

MR. GORMAN: I think that is a very difficult question for people as inexperienced as ourselves to make an observation on, but I would venture to say that I could get that information.

MR. STEWART: Subject, Mr. Gorman, to what the Chairman says, that might be the way to leave it. If you would care to let the Commission have your comments on that situation I think it would be very helpful, because really what we are here for is to try to assess this properly.

THE CHAIRMAN: Yes. I think, Mr. Stewart, if Mr. Gorman is going to do that he may just as well not restrict himself to the one level you have spoken of and in the circumstances in which you have directed your question. I think that Mr. Gorman may like to look at it a little more carefully before he agrees with it.

When he looks at it having regard to $4,000, he may like to look at it having regard to $2,000 and $10,000, and if he would we would be very happy to hear from him.

MR. GORMAN: Yes.

MR. STEWART: There are all sorts of things which come into this, and when we think of the average

member of a co-operative, the $4,000 taxable income figure is too high; and, as I have already said, the 22% rate, in any event, is an incremental rate rather than an effective rate. That is another factor to be taken into account.

But I think basically one of the points which I would suggest you might consider is this: that perhaps what is really involved here is a question of tax rates, and also a question of whether or not adequate credit against one's personal tax is given for the corporate income tax which is paid. That is why I prefaced this by a reference to your suggestion that corporate tax rates be reduced, because if we are thinking of someone whose effective corporate rate is close to 52%, obviously a 20% dividend tax credit is not altogether effective, but the more the 52% rate can be reduced, then the less double taxation of corporate income, it seems to me, we have.

In other words, putting it this way: in the case of the commercial corporation, one of your members, there is at the moment a minimum corporate tax of 18%, or 23%, call it what you will; in the case of the co-operative there is no such tax now. There is this 3% tax on capital employed.

MR. ROLLING: Right.

MR. STEWART: But there is the tax on patronage dividends, and the representations you make in your brief, it seems to me, will be strengthened or weakened according to whether the two sets of taxation are comparable or far apart in their results.

You see, I am really, I think, questioning you

about your statement on page 20 which I have already referred to, that "the contribution of the individual corporation and its shareholders is several times as great as that of the co-operative group."

EMT/ss

Now, I would not dispute for a moment if you are talking about a large cooperative such as the wholesale cooperative referred to later on. It is true, but if you take what may be a more typical case, take the commercial corporation on the one hand with taxable income of $25,000.00, and a cooperative on the other hand with income of $25,000.00, what are the comparative incidences of income taxation? That is an attempt, Mr. Chairman, to state the question, and what the answer is I do not profess to know. I am just raising the point.

MR. ROLLING: You made one statement in your explanation there that patronage dividends were taxable. You meant in the hands of the recipients?

MR. STEWART: Yes.

MR. ROLLING: Our contention, of course, on the part of taxation is that the present context of the 20% tax credit should apply in both cases, both corporation and cooperative.

MR. STEWART: Yes, I think your brief is very clear in that. Now, I suggest the cooperative corporation is taxed on its income the same way as the ordinary corporation.

MR. ROLLING: Right.

MR. STEWART: Then the present dividend tax credit should be extended to the patronage dividends.

MR. ROLLING: Yes.

MR. STEWART: Patronage dividends then would be paid after what was left after tax. Now, would you also in your considering that and letting us have your views,

keep in mind the distinction between types of cooperatives in this connection, because in Section 75, Subsection 6, patronage dividends are taxable except in certain cases. You will observe the words in brackets in the Subsection we do not bring into tax or into income for tax purposes patronage dividends which represent allocations in respect of consumer goods or services.

Now, there is another feature of your brief which I would like to canvass with you to some extent. You refer to the fact that when these patronage dividends are credited to shareholders' accounts, they are in fact available for the operations of their cooperative and/or the expansion of the business of the cooperative. Am I not correct?

MR. ROLLING: Yes.

MR. STEWART: I would like to put this to you: In the case of a commercial corporation, once the corporate income tax is paid, there is nothing to compel the payment of dividends or to prevent, if you like, the accumulation of surplus. If the shareholders wish to avoid the disadvantage, potential disadvantage of a large surplus accumulation, they can distribute their earnings and reinvest what they received by way of dividend in the corporation. In any event, our corporations do accumulate earnings, and as I say, there is nothing in our law at the present time which requires them to make any distribution whatever.

MR. ROLLING: Right.

MR. STEWART: Now, in those circumstances is there really discrimination in favour of the cooperative,

because what is happening, as I see it, is that the cooperative is allocating its earnings, a substantial portion of them, to shareholders' or members' accounts and the members do not choose to withdraw those credits in many cases, and is the result not the same as though the shareholders, the members were receiving and reinvesting the earnings? This is exactly what can happen in the case of a commercial corporation.

MR. ROLLING: But if it is continued in a commercial corporation for a protracted period of time, you might have difficulty or experience difficulty in getting investors to invest in the corporation itself. This is one point.

The second point is although a co-op may dispense some cash in the form of patronage dividends, they may also give out a share credit of some type at the same time, and the purchases of the individual may or may not be concerned in the particular case, whereas with a corporation, usually the shareholder who might be subject to what you suggest here, of course, may not be an investor of the corporation but an investor there.

MR. STEWART: Yes, but Mr. Rolling, you have conceded you have no objection to the cooperative form of organization.

MR. ROLLING: That is right.

MR. STEWART: And therefore the distribution of earnings on a patronage basis. Now, let us just look at this question about the difficulty of obtaining the investment. I take it that in the case of your average member who is a small retailer, the number of shareholders

of the company is going to be quite small. Chances are that these corporations will be owned by members of one family or by a comparatively small group of people. Would that not be correct?

MR. ROLLING: That is true.

MR. STEWART: All right. If they do not want to run the risk, as I said before, of surplus accumulations, can they not distribute earnings year by year, that or loan money back to the corporation or take up additional shares, whether they are redeemable preferred shares or additional common shares?

MR. ROLLING: Well, they might by mutual agreement, but not necessarily by regulation as in the confines of that organization which you suggest as being members of one family.

MR. STEWART: I agree that you would have to have a decision on the part of the board of directors.

MR. ROLLING: Yes.

MR. STEWART: That the monies be distributed.

MR. ROLLING: Yes.

MR. STEWART: Then you would have to have agreement on the part of the recipients of dividends that they would reinvest them. However, is it not the fact that in the case of a cooperative, either immediately or after a decent interval, the member can take away or take out what is deposited or what is credited to his account?

MR. ROLLING: I refer you to page 22 of our submission. Perhaps this would answer. In the last paragraph there:

"Through the years Federated has consistently

reinvested a major proportion of the earnings rather than pay out in the form of patronage refunds.

'During the period 1947 to 1957, patronage refunds were paid by two-thirds in certificates of indebtedness and one-third in common shares. Since 1958, patronage refunds were paid only in the form of common shares. Cash returns to the members have been achieved by revolving certificates and repurchasing shares'."

MR. STEWART: But is it not the fact, Mr. Rolling, under the provisions of Section 75 ---

MR. ROLLING: Yes.

MR. STEWART: That if a cooperative wishes to make a deduction in respect of patronage dividends in one year it must release a corresponding amount held back from previous years to its members?

MR. ROLLING: This is stated as that in the Act. You are thinking now of (a) and (b) and 1 and 2 of 75? 75 (1) and (2).

MR. STEWART: Yes. That is the governing section.

MR. ROLLING: Right.

MR. STEWART: You are permitted there to make deductions pursuant to allocations in proportion to patronage. Then if you observe Section 75, Subsection 4, there is a definition of the expression, allocations in proportion to patronage. That is a somewhat involved definition.

MR. ROLLING: Right.

MR. STEWART: Then I think I should refer also to the use of the term payment in Section 75 (1), what you can deduct as a payment, and the expression payment is defined in Section 75, Subsection 4, paragraph (f). There if you issue a certificate of indebtedness or shares that constitutes a payment if the taxpayer has in the year or within twelve months thereafter disbursed an amount of money equal to the aggregate face value of all certificates or shares so issued in the course of redeeming or purchasing certificates of indebtedness or shares of the taxpayer previously issued.

Now, that seems to contemplate a sort of revolving type of payment?

MR. ROLLING: That is correct. We refer to that in our brief too.

MR. STEWART: And then we go on to Subsection 2, and we find payment includes the application by the cooperative of an amount to a member's liability to the taxpayer pursuant to a bylaw of the taxpayer pursuant to statutory authority at the request of the member.

What I am suggesting is that these amounts which are credited to the members' accounts are not frozen there for an indefinite period, but that the member can in due course withdraw them from the cooperative.

2 MR. ROLLING: In most cases you would be correct, but this is not always the case. The funds are there and are available for use.

MR. STEWART: And are they not there simply for a period?

MR. ROLLING: Yes. That is stated within the

limitations of the Act.

MR. STEWART: So that again it seems to me there may not be a tremendous difference.

MR. ROLLING: They do not pay the corporation tax.

MR. STEWART: Quite so, but we have already discussed that aspect of it.

MR. ROLLING: Yes.

MR. STEWART: And you are going to consider whether the incidence of income tax on the one is in fact greater than the incidence of income tax on the other?

MR. ROLLING: Right.

MR. STEWART: Leaving aside the question of the corporate income tax, what I am now suggesting to you is that it may be that earnings can be accumulated by commercial corporations just as readily as they can be by cooperatives.

MR. ROLLING: I do not think they can under the present regulations. Can you give me an example, sir?

MR. STEWART: Well, I think in the case of commercial corporations ---

MR. ROLLING: No dividends you mean?

MR. STEWART: The position is quite clear if I understand it correctly. Let us suppose that we have a commercial corporation which has an income, a taxable income of $10,000.00 in a particular year. Its corporate tax rate is 23%, $2,300.00, so that if it has $7,700.00 left, so far as I am aware the shareholders of that corporation can leave that $7,700.00 there as long as they like. However, if they choose to distribute the $7,700.00

by way of dividends, loan the money back to the corporation or reinvest it in shares of the corporation, there is nothing whatever to prevent them from doing it, so that the $7,700.00 can remain effectively working for the corporation indefinitely.

C/dpw

MR. ROLLING: Subject, of course, to tax and what it earns.

MR. STEWART: That is right. If they pump the money back in, if they leave the money or if they pump it back in, then presumably the future earnings of the corporation will increase and the corporation, among other things, will pay additional corporate income tax. We are back on the question of whether this corporate income tax should be extended to co-operatives.

MR. ROLLING: That is right. We suggest that.

THE CHAIRMAN: Have you come to the end of that particular subject? If so, we will break.

MR. STEWART: Yes.

THE CHAIRMAN: We will stand down for ten minutes.

--- Short Recess

THE CHAIRMAN: Mr. Stewart, will you continue?

MR. STEWART: Thank you, Mr. Chairman. Mr. Gorman and Mr. Rolling, I would like to come to a slightly different subject. So far as the ordinary commercial corporation is concerned would you see any problem about providing, when dividends are paid, they will be subject to a deduction at the source by way of tax of, say, 15 or 20 per cent?

MR. ROLLING: Would you rephrase that?

MR. STEWART: At the present time, in the case of a Canadian corporation, as you know, if you are paying a dividend to a non-resident shareholder it is subject to

what we call a withholding tax of 15%. Now, dividends which are paid to Canadian residents are not subject to any similar withholding; similarly, as far as I am aware, patronage dividends which are paid by co-operatives are not subject to any withholding.

What I am really asking you is: what would your comment be to a proposal, what would your reaction be to a proposal that both dividends and patronage dividends paid to residents of Canada be subject to a tax deduction at the source of, say, 15 or 20 per cent?

MR. GORMAN: This is something that we had not considered in our Committee when we were preparing this brief, Mr. Chairman, and I, for one, don't feel qualified as an individual to express an opinion on it. On the face of it it seems like a reasonable suggestion.

THE CHAIRMAN: I think that is fair. We cannot expect you to go very far beyond what you have put before us.

MR. STEWART: Now then, gentlemen, you have made reference to a company called Federated Co-Operatives Limited, which is referred to on pages 22 and 23 of your brief. This appears to be a substantial concern. Do I take it that you have seen its financial statements?

MR. ROLLING: Yes, these are published figures.

MR. STEWART: Published in the daily press?

MR. ROLLING: No, they are available to ourselves through our Dominion Association.

MR. STEWART: Now this, in any event, is a wholesale co-operative and it serves, according to what you say at the top of page 22, it serves retail stores, members

on the Prairies.

Now, I would just like to be sure I can follow through what happens to the income of this wholesale co-operative. You indicate that it pays out a substantial part of its earnings by way of patronage refunds and I take it that those patronage refunds or payments would go to these retail store members. Are those retail store members commercial companies or are they those co-operatives?

MR. ROLLING: They are co-operatives.

MR. STEWART: So that what they receive, in effect, increases their income and would be passed on by them in whole or in part to their own individual members.

MR. ROLLING: If they declared patronage dividend, yes.

MR. STEWART: Have you considered whether there would be any merit in having one set of rules for large companies of this type, large co-operatives of this type, and another set of rules for small co-operatives or do you lump them all together for your purposes?

MR. ROLLING: All together, sir.

MR. STEWART: Now, on page 39 of your brief, you deal with the general subject of co-operative sales of merchandise and supplies. I would like to refer, again, to a publication I think I have already mentioned called Recent Growth in the Canadian Co-Operatives, by Professor R. Craig McIvor, which was published by the Canadian Tax Foundation in 1962. The first article in that book is one which bears the same name as the book itself. On page 24 of that book, dealing with merchandising

co-operatives, Professor McIvor indicates that in recent years those co-operatives have grown in certain particular fields.

If I might read from the bottom of page 24, he says this:

> "Lengthy statistical comparisons are indeed tedious and need not in this area be carried further. They serve to establish two main points. (1) That in particular areas of merchandising, as for example feed and fertilizers, hardware, lumber, clothing and home furnishings, the rate of growth in co-operative sales has substantially exceeded those in the whole economy; and (2) at the present stage of development total co-operative merchandising sales represent a very small but obviously increasing percentage of total Canadian sales in the comparable areas."

Then in a footnote to that portion that I have read he says that it appears highly unlikely on the basis of earlier post-war calculations that the co-operative portion of retail merchandising sales in Canada would have amounted at the end of 1960 to more than 3%. I think that figure of 3% also appears in your brief at a slightly later stage.

Now, would you agree as of that, as of the end of 1960, the figure of 3% was approximately correct?

MR. ROLLING: Yes, I believe it was at that time.

MR. STEWART: Now, that seems a pretty low proportion of retail sales to cause you particular concern. 2 Is your concern based on the apprehension that the percentage may continue to increase?

MR. ROLLING: It has continued to increase, I believe.

MR. STEWART: And you think this process may go on?

MR. ROLLING: I would think so, yes.

MR. STEWART: Well, then, on page 25, dealing with ---

MR. ROLLING: Pardon me. To substantiate that, going back to page 39, we refer there to merchandising sales, the period 1957-1961. This compares with an increase of 12.3 in the retail trade in Canada for the same period and No. 4, 15.6% for the wholesale trade, which indicates it is increasing.

MR. STEWART: On page 25 of Professor McIvor's article he also suggests that between 1953 and 1960 in the wholesale trade that co-operative sales rose from approximately 2% of total Canadian wholesale trade in the relative commodity classification to approximately 3%. Actually, you have quoted that sentence at the bottom of page 41. That, again, would be substantially accurate as far as you know.

MR. ROLLING: As far as I know, sir.

MR. STEWART: Now, on page 47 of your brief, at the end of the first paragraph, where you have been discussing what you consider to be an inequitable tax situation, you say that this involves - then it is the

next few words I would like to ask you about - involves the misallocation of the nation's resources.

MR.ROLLING: To answer that I would like to quote the author of The Recent Growth in Canadian Co-Operatives.

MR. STEWART: What page is this?

MR. ROLLING: This goes back to page 39 and I believe page 25.

MR. STEWART: You mean page 39 on your brief?

MR. ROLLING: Page 39, where I was at, and the other page 47 you referred us to.

COMMISSIONER WALLS: I believe it is covered by a footnote on page 40, page 24 on the book you have in front of you.

FF/ss

MR. ROLLING: I can't give you the reference of Prof. McIvor's quotation there for the moment, if you would be patient on that.

Could I read the quotation?

MR. STEWART: Please do.

MR. ROLLING: "The author of 'Recent Growth in Canadian Co-operatives', after pointing out the discriminations which existed in favour of co-operatives under their tax laws has drawn attention to the misallocations of our national resources which resulted from the discrimination as follows:

If this " --- the author is referring to the extraordinary rate of growth which cooperatives enjoy --- "is correct, then the present tax arrangements are undesirable."

MR. STEWART: May I ask what you are reading from?

MR. ROLLING: I am reading from this quotation or commentary by Prof. McIvor. I haven't given you the reference; I have to locate it.

MR. STEWART: What you are reading from appears to be a report on Prof. McIvor's book.

MR. ROLLING: Yes. I haven't got the reference.

MR. STEWART: I notice on page 38 of Prof. McIvor's article in the last paragraph, the second sentence, he says: "There is nevertheless, a very good case on the grounds of its effects upon equity, competitive advantage, efficiency in resource allocation and upon public revenue for a re-examination and reorganization of this particular

piece of legislation."

Now, when you talk about misallocation of the nation's resources, are you on the same point as is made there, that is efficiency in resource allocation?

MR. ROLLING: I would think that would be correct. The financial advantage enjoyed by one against the other would reflect the amounts available to the treasury.

MR. STEWART: Thank you. And this is something, I take it, then, that is a national matter as opposed to a regional matter, and it is a problem relating to industry as a whole and not simply to a particular industry.

MR. ROLLING: It would relate to all, sir.

MR. STEWART: Now, gentlemen, let us suppose for the moment that your proposals were adopted and that the Government in its wisdom chose to tax cooperatives as ordinary corporations, what effect do you consider that this would be likely to have on the cooperative movement?

Let me break that general question down into a number of sub-questions. First of all, do you think that if cooperatives generally were subject to the present rate of corporate tax they would or could proceed with what I believe they call pricing out? Are you familiar with this?

MR. ROLLING: Not that one, no. I think I follow what you are getting at.

MR. STEWART: In the case of a merchandising cooperative, instead of selling at ordinary commercial prices or the equivalent they might sell at reduced prices,

and thereby reduce their profit.

MR. GORMAN: I don't think that would create a problem. This is happening today in discount operations.

MR. STEWART: So so far as you are concerned, do I gather that you think they would adopt that technique or could adopt that technique?

MR. GORMAN: Well, Mr. Chairman, it is our contention that cooperatives are in business to make a profit, and if they are going to continue in business to make a profit, they could not adopt that technique any more than private business could and remain in business.

MR. STEWART: We have been faced with --- I won't say threats, but with suggestions that these pricing out techniques are available as recently as this morning, although I grant you that the suggestions there came from credit unions and not cooperatives in the strict sense. Do I infer that you would not take suggestions of this nature seriously?

MR. GORMAN: No.

MR. STEWART: You would not?

MR. GORMAN: No.

THE CHAIRMAN: This is the point I think they answer on pages 30 and 31 under the heading "Price Adjustment Theory." Do you think that would be the case, Mr. Stewart?

MR. STEWART: I think that is probably so, Mr. Chairman.

Perhaps we can ask the witnesses. Is what you say under the heading "Price Adjustment Theory" commencing on page 30, is that your answer to the pricing out argument?

MR. GORMAN: Yes, I would say it is.

MR. ROLLING: Yes, I think so.

MR. GORMAN: Yes, substantially, Mr. Chairman.

THE CHAIRMAN: I wish that connected, Mr. Stewart, because there is an important question I would like to raise when you are through, not now.

MR. STEWART: Does what you say there deal with the question of pricing out? As I understand what appears on page 30 where you are talking about a price adjustment theory, you are complaining about the fact that cooperatives say that they are carrying on business at cost and what is rebate or refund or what they pay by way of patronage dividends to their members is simply an adjustment to bring transactions to what was regarded as the original cost basis. I think my question is somewhat different. What I am getting at is this: Would they price out in this sense? Let's suppose, to take a simple example, that the price of a pair of socks is 39 cents and that ultimately the person who buys a pair of socks gets a one-cent refund or rebate. Now, suppose, faced with this problem of income tax on cooperatives, the cooperative decides to sell that pair of socks not at 39 cents, but at 38 cents so that it is operating as closely as it can to a break-even point and its patronage dividands are reduced to an absolute minimum, do you envisage that the imposition of income tax on cooperatives might result in that type of costing technique or pricing technique?

MR. ROLLING: This would, as you suggest, appear to defeat the purpose of all cooperatives, which I understand are organized to increase gain for their members.

Do you suggest that this would cause them not to operate to a point of gain for their members?

MR. STEWART: Fortunately, Mr. Rolling, I am not in a position to answer questions.

MR. ROLLING: Pardon me; I wanted to be sure I fully comprehended yours. But I would suggest to you that the cooperatives are organized to increase the gain of their members and, as you suggest, I do not see how this would be possible, as you said, a break-even point, and this would obviously eliminate even patronage dividends. Is that correct?

MR. STEWART: Well, Mr. Rolling, I am not sure that a person who was a member of a cooperative would agree that the object of a cooperative is gain for its members. I think what they might suggest is that they are banded together to accomplish in concert and in effect on a cost basis things which they cannot do individually. So that while, as a matter of practice, and I suppose to some extent because they deal with non-members, they do sell --- and I am talking about merchandising cooperatives --- at sort of normal market prices, they then proceed to restore their membership to a cost method of operation through the device of a patronage dividend.

MR. ROLLING: Well, my concept is that each member is a joint venturer in a corporate business as a shareholder in a co-op, and I do not believe they would be too happy with what you suggest, even though they have banded together for what may be termed their betterment.

MR. STEWART: Well, your approach to corporate

organization is the traditional commercial approach, but I am not sure myself it is the cooperative approach. But thisis something we don't have to decide here.

I think, however, this question is pertinent. Do you consider that it is in the interest of the average retail merchant in Canada or in Ontario --- let's confine it to Ontario --- to encourage cooperatives to sell on a cost basis as opposed to the ordinary commercial basis?

MR. ROLLING: I think this might clarify that particular point. On page 26, we have an example of a man in the retail business and a cooperative in the grocery trade, both of them showing a net profit of $10,000.00 at the end of the year. The cooperative in the grocery trade with the net profit --- this is to the left of the page --- of $10,000.00 less patronage
2 dividends also paid in full or partly retained in the business $7,500.00, taxable profit of $2,500.00, tax payable, Federal and Provincial, $575.00, as against an individual retailer with a net profit of $10,000.00, on the right of the page, less personal allowances of $2,500.00, taxable profit of $7,500.00, tax payable (after giving effect to Federal and Provincial adjustments), $1,483. 20.

I believe that is a reasonable comparison to the feeling of the retailer that wouldn't necessarily want to encourage competition of that type.

MR. STEWART: Well, Mr. Rolling, I understand your Table on page 26, but I don't think that really answers the question I have put to you.

Let me give you a simpler example.. Suppose one

of your members is actively engaged in competition with a cooperative in his own town and at the present time they are both selling a particular type of tooth powder for 59 cents, and, as a result of your representations and such other factors that it takes into account, the Government decides that it will tax cooperatives on their income and the cooperative that we are presently concerned with, the competitor of your member, decides that it will operate as close to a cost basis as it can, and one of the results of this is that the price of tooth powder in the cooperative store is cut from 59 cents to 57 cents.

Is there something that you as members of your Association would contemplate with equanimity?

MR. ROLLING: I would say that no retailer to our knowledge appears in normal competition such as that.

MR. STEWART: So in substance your view is if cooperatives do price out, the independent merchant can satisfactorily compete against him.

MR. ROLLING: I would say so; yes, sir.

MR. STEWART: And that would mean, presumably, that you would not expect that a substantial volume of business would be diverted from the independent retail merchant to the cooperative.

MR. ROLLING: No, sir.

GG/ET/dpw

MR. STEWART: Now, gentlemen, as you know, under the present legislation co-operatives are subject in certain events to a tax of 3% on capital employed. I appreciate that your representations are designed to alter the present situation quite materially, but suppose for the moment we were considering a retention of the basic system that we now have, have you any comments to make on the 3% figure?

MR. ROLLING: I don't think so, sir.

MR. GORMAN: It is a very minimal figure, Mr. Chairman. If we were to consider the example we show on page 26 to show profit of $10,000, 3% on his investment, it is a small tax; an investment, perhaps, of $20,000, 3%, $600, it doesn't change too much from the present tax that we show in that example for that same merchant.

MR. STEWART: But you have no particular suggestion to make as to a figure which might replace the 3%?

MR. GORMAN: It is quite within the realm of possibility, Mr. Chairman, that the Dominion Association, the Retail Merchants' Association, with the help of Professor Lloyd Barber of the University of Saskatchewan, when they make their presentation in the Fall some of the points we have failed to bring out may be further elaborated on or more detailed.

MR. STEWART: Thank you. Incidentally, if I could go back for a moment to page 24 of your brief, in the third paragraph on that page you deal with the tax payable by a co-operative in certain events. You indicate there that on those figures the co-operative would pay 7.9% of its earnings by way of tax.

2

Is it not the fact that that particular co-operative is assumed to have paid out or to have paid in patronage dividends a total of $150,000, which would be taxable in the hands of the recipients?

MR. ROLLING: If they were in a tax-paying bracket.

MR. STEWART: Yes. By the same token a commercial corporation is taxed on dividends only if he is in a taxable bracket.

MR. ROLLING: Correct.

MR. STEWART: Similarly, on page 26, where you set out another comparative example, you show tax payable by the co-operative, on the lefthand side of the page, of $575, but you have not taken into account any tax payable on the patronage dividends.

MR. ROLLING: No.

MR. STEWART: Now, gentlemen, in your brief there does not appear, if I remember correctly, to be any particular point made about the accumulation of reserves by co-operatives or about the accumulation of investments and therefore investment income by co-operatives. Have you any particular comment on either or both of those points at this stage?

MR. ROLLING: I would refer you to page 23, where we give a statement there that from 1954 to 1962 on the financing and growth of this particular co-op as it commenced moving across the country from Saskatchewan to Manitoba in 1955 and through 1962 finally to Alberta with a total of $94,825,852.

MR. STEWART: Those are sales?

MR. ROLLING: Yes, correct.

MR. STEWART: And you refer about halfway down that page 23 ---

MR. ROLLING: In paragraph 2.

MR. STEWART: Yes.

MR. ROLLING: To the example of aggregate operating savings from 1947 to 1961 were $27,651,000.

MR. STEWART: Then you go on and say that from 1948 to 1962 equities in common shares, certificates of indebtedness and reserves increased by some $15,596,000?

MR. ROLLING: Correct. Therefore, about $12,055,000 was paid in income taxes and cash dividends. However, we do qualify that that is a general statement.

MR. STEWART: This is one particular case, and there, of course, we are not able from what you say, at any rate, to break down that $15,500,000 between common shares on the one hand and certificates of indebtedness on the other hand and reserves in the third place. Your researches into these co-operatives have not led you to form any particular general conclusions about the amounts of their reserves?

MR. ROLLING: No, but I could make probably an observation in that regard with regard to Federated Co-Ops, that it would appear as though they have minimized their income tax liability to less than 5% in 1961. To the best of our knowledge this procedure is consistent with long-term policy. It can then be estimated with reasonable accuracy that their cash payments on aggregate operating savings of $27,651,000 from 1947 to 1961, referred to on page 23, the second paragraph, are not likely to have been

in excess of one million dollars.

Therefore, in addition to the increase of $15,596,000 in equities, by way of re-investment of patronage dividends, approximately $11,000,000 would appear to have been distributed to members in the form of cash returns. That is an observation.

MR. STEWART: I see. Well now, Federated Co-Operatives, as we have said earlier, is a wholesale co-operative. I asked the question earlier whether you would draw a distinction between large co-operatives and small, and you indicated that you would lump them all together. Perhaps I might ask a supplemental question: would you draw a distinction between co-operatives which deal direct with the producer or the consumer on the one hand and these wholesales or national organizations on the other?

MR. GORMAN: Those two types of co-operatives, Mr. Chairman, I think, are fairly akin and as against the agency type of co-op.

MR. STEWART: Well, do you consider that the first group, that is the wholesales and the national, because of the fact that they deal with co-operatives as opposed to dealing with individuals should be singled out for any special treatment for tax purposes?

MR. ROLLING: No.

MR. STEWART: Again, you lump all co-operatives together?

MR. ROLLING: Right.

MR. STEWART: Gentlemen, I think those are all the questions I have at this stage.

THE CHAIRMAN: Thank you, Mr. Stewart. I have one or two questions and I guess the other Commissioners have likewise, and we will be late. On page 31, I would like to draw attention to the price adjustment theory in the second to last sentence of the top paragraph which reads: "But the patronage dividend is not paid to the person or firm from which the gain is derived."

In order to qualify the dividend must be proportionate to patronage, and I would have thought that that is the best attempt that could be made of allocating the dividend to the person or firm from which the gain is derived. I wish you would expand on those words and tell me what meaning, if any, I have missed.

MR. ROLLING: Perhaps I could answer that in this way from Robert G. Patterson's book, "Tax Exemptions of Co-Operatives" on that statement. There is no clear-cut difference between patronage dividends in general and dividends of ordinary corporations. The fact that patronage dividends are paid to patrons who are also stockholders does not make them anything other than a distribution of profits. Now, does that answer your question, Mr. Chairman?

THE CHAIRMAN: No, I do not think so.

MR. ROLLING: Well, I could add further, then, that patronage dividend is not paid to the person or firm from which the gain is derived in an analysis of the taxability of co-operative earnings or net margins. The significance of this point cannot be over-emphasized.

2 Now, that is a quotation from Robert G. Patterson's book, "Tax Exemption of Co-Operatives," page 71.

THE CHAIRMAN: Yes. That is your answer, is it?

MR. ROLLING: Right.

THE CHAIRMAN: Thank you very much. I was hoping that you might include in your submission a reference to the shrinkage of the tax base in this area because of the fact that there is a large increase in the business of co-operatives, and you might give some indication of the business failures or the take-overs of private enterprise by co-operatives if, in fact, that has occurred. I would suspect there may have been failures and there may have been take-overs if there has been a decided advantage to the one type of organization as opposed to the other.

HH/MC/ss

MR. ROLLING: I cannot quote examples, but there have been cases where funds have been available to take over a retailer and buy a Co-op, as you bore out.

THE CHAIRMAN: Has that not operated in both ways, have non-cooperative businesses taken over cooperatives?

MR. ROLLING: Never that I have known, Mr. Carter.

COMMISSIONER GRANT: I wonder if you would make any comment on the fact that in the United States as recently, I think, as 1961, legislation was passed which puts the Cooperative movement in that country on much the same basis tax-wise as we have in Canada. There is one exception to it and that is in order to take patronage dividends from earnings before arriving at net taxable figure that 20% of that patronage dividend must be paid in cash. I am interested in your reaction to (a) the fact that the legislation in the United States is quite recent, modelled as it is on legislation which has been in our tax laws for two decades almost and also the fact that they have made that one modification that 20% must be paid in cash. Their idea stated openly, I believe, is that the earnings of Cooperatives should not be subject to double taxation.

MR. ROLLING: I am not sure, Mr. Grant, but I believe you are referring to the year 1947, and the year 1951 in the United States?

COMMISSIONER GRANT: No.

MR. ROLLING: Quite recent?

COMMISSIONER GRANT: Quite recent.

MR. ROLLING: I would not be prepared to answer that question. In view of the fact I am a member of a Committee I would like to make a note of it and reply in writing.

COMMISSIONER. GRANT: Yes, that would be satisfactory.

COMMISSIONER WALLS: It is not too important a question, but I would like to clarify it forthe record. First of all, as appears in your synopsis on page A you state industrially the retail industry contributes heavily to the Federal treasury at the income tax level apart from its involvement with Federal excise and sales tax,and on Page 6, paragraph 6, you say that retailers are heavy contributors to the Federal treasury on the income tax level separate and apart from payment of Federal excise and sales tax on their stock-in-trade.

By these statements do you mean the retailers are paying Federal sales and excise tax?

MR.GORMAN: Mr. Chairman, yes, to some extent they are. If the retailer buys $100.00 worth of merchandise, and much of the merchandise that many of us carry is very fragile in nature, and if it happens to be very valuable glass, for the sake of argument, and that falls on the floor, there is no recapture for that. In the meantime the retailer has paid.

COMMISSIONER WALLS: Is it not a fact the manufacturer has paid the sales tax and the excise tax or the licensed wholesaler pays the excise and sales tax?

MR. GORMAN: That subsequently is invoiced to the retailer.

COMMISSIONER WALLS: Therefore is it not equally

applicable to the Cooperatives? Do they then not indirectly also pay the same tax?

MR. GORMAN: Yes, I would say it would.

COMMISSIONER WALLS: We have had some participants in front of us who are pointing to this as being a negative position for the retailer. They claim that indirectly the retailer has made a profit through pyramiding of this tax. In other words, if you buy a product with the sales tax added and you put the percentage of profit on it, then that percentage is added to both the product and the sales tax. Do you agree with that?

MR. GORMAN: That is right, that is the practice.

COMMISSIONER WALLS: There is just one other question I had in mind, and that was the last paragraph you quoted on page 23 of the rapid growth of this one particular cooperative group. It is a Federated group and suddenly has sales of 14 million in one year in Alberta with nothing shown for previous years. Could that not be because it has federated an already existing cooperative organization in Alberta into its organization and therefore it is not real growth, but that same organization could have had like sales in the previous years.

MR. ROLLING: Mr. Walls, this would be difficult to answer without some further diagnosis of this statement. It is entirely conceivable the amount might have been as you suggest, inherited from the same amount of business last year, but it is also possible that this is business that might have been done within the year, as shown on our chart in 1962. We would have to, I believe, be very fair and put down your question and see if we can answer that

one in writing, Mr. Walls.

COMMISSIONER WALLS: Thank you very much.

THE CHAIRMAN: Thank you very much, Mr. Gorman and Mr. Rolling, for your help this afternoon. This matter of cooperatives is an extremely difficult one. This is not quite our start on it, but we haven't got into it very far so far.

It is not the only problem, of course, that we are confronted with. There are many important ones. While we appreciate your assistance tremendously on this aspect, there are others we would like to hear about from the retail merchants. For instance, it has been suggested to us that sales tax might be all shifted to the retail level. Undoubtedly you have heard that suggestion. I cannot think of any group that would be more concerned over a shift in the point at which sales tax would be applied than the retail merchants of Ontario and Canada.

You are undoubtedly aware of other proposals which we have had made to us already which would concern the retail merchants. We do hope that either through your written submission or through your national organization that you will express your views, not just on cooperatives, although we want those, but on other matters that will weigh with your people.

We need all the help we can get. We need help particularly from those people who are concerned. I know there are many items that will concern you.

Thank you very much indeed for your attendance this afternoon and your excellent written submission and

for submitting yourselves to a barrage of questions. If we have seemed to be a little vigorous at times in our questioning, it is only to better understand the problem you have presented to us. Thank you very much indeed.

MR. GORMAN: It is our pleasure, sir.

THE CHAIRMAN: Mr. Secretary, is there anything else today?

THE SECRETARY: There is nothing else today. At 9:30 tomorrow morning the Federated Council of Sales
2 Finance Companies, Mr. J. S. Robbins of Dundas, Ontario, and
Mr. Hamilton Cassels on behalf of the University of Toronto.

THE CHAIRMAN: We will stand over until 9:30 tomorrow morning.

---Adjournment.

ROYAL COMMISSION

ON

TAXATION

HEARINGS

HELD AT
TORONTO
ONT.

VOLUME No.: 25

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ROYAL COMMISSION ON TAXATION

Hearing held in Howard Ferguson Auditorium, Sir Daniel Wilson Residence of University College, University of Toronto, Toronto, Ontario, on Wednesday, the 22nd day of May, 1963.

COMMISSION:

MR. KENNETH LeM. CARTER -- Chairman

MR. J. HARVEY PERRY

MR. A. EMILE BEAUVAIS

MR. DONALD G. GRANT

MRS. S.M. MILNE

MR. CHARLES E.S. WALLS

LEGAL ADVISER:

MR. J.L. STEWART, Q.C.

RESEARCH DIRECTOR:

PROF. D.G. HARTLE

SECRETARY:

MR. G.L. BENNETT

ROYAL COMMISSION ON TAXATION

HEARINGS HELD AT THE CITY OF TORONTO, ONTARIO

May 22, I963

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Toronto, Ontario,
Wednesday,
May 22nd, 1963.

/dpw

--- On commencing at 9.30 a.m.

THE CHAIRMAN: Mr. Secretary, it is just about 9.30. I think we might start.

THE SECRETARY: All right, Mr. Chairman, Commissioners. You will recall, Mr. Commissioners, that in Montreal we entered into the records as Exhibit No. 19 the brief of the Federated Council of Sales Finance Companies. At this time the officers of the Council are appearing before you and wish to speak to the brief which has already been entered.

Mr. E.M. Howarth, Executive Vice-President, will speak to the brief. On Mr. Howarth's left is Mr. K.J. Doig, Vice-President, Finance, Industrial Acceptance Corporation Limited, a member of the Council, and on Mr. Howarth's right is Mr. E.G. Jarmain, Treasurer, Canadian Acceptance Corporation Limited, another member company of the Council.

THE CHAIRMAN: Thank you, Mr. Secretary. Good morning, gentlemen. We are very glad to have you here this morning, and we are grateful for your attendance. It is not necessary nor desirable to read to us your submission. We have had an opportunity of going over it, which we have done, and we are very much interested in the contents. Most of our visitors speak to their submission, either summarizing it or commenting on it, and we are quite prepared to ask a few questions.

It seems to me, Mr. Howarth, this lends itself to dealing separately with each of the three points which you have raised. They are not particularly interrelated;

2 I think each point stands by itself. I think you have pretty well covered the Federated Council in your submission and your relationship to it. We would be very glad to hear anything you would care to say to us.

MR. HOWARTH: Thank you, Mr. Chairman and Commissioners. I do not think I will endeavour to review the brief for its main points again for it is a fairly short one and I am sure you will have a chance to consider it. I think, perhaps, I could just add one word about our Council. That is, while we have 39 member companies, they do vary considerably in size and also in geographical position, and to some extent, in the type of business that they conduct, although they are in the sales finance field.

We did wonder when we considered our appearance here this morning just how many companies we should ask to be represented to give a broad picture of our affairs such as you would wish to discuss, and we came to the conclusion that we would appear in rather a small group and if something should arise in the discussion where we felt it went beyond either the Council's accumulated experience or the experience of the gentlemen who are with me this morning, then we would make that point with you and possibly have to refer for additional information if this should arise.

Mr. Doig and Mr. Jarmain are here on behalf of the Council to speak from firsthand experience on any of these affairs. I think the only thing I would say is that I understand in the discussion we are free to comment and to add to each other's remarks if we feel that this is necessary. Is this the procedure?

THE CHAIRMAN: By all means. I do not think you

could have had a complete representation because you are growing so fast, I observe, and you have increased by one since you wrote this submission. By all means feel free to express any opinion.

MR. HOWARTH: I think we would prefer to consider any questions or comments that you or your Commissioners might wish to make and proceed from there.

THE CHAIRMAN: Well, we will start with the first of the headings that you put to us; namely, credit unions. You recommend that seeing they have become, you say, commercial in character, this Commission should consider whether it is in the best interests of the Canadian economy that they be exempted from carrying a fair share of the tax burden. Your suggestion, I think, is that they should be taxed in the same way as any other corporation; is that correct?

MR. HOWARTH: That is our basic recommendation. I think that we, as an industry, would consider that co-operatives of any kind and credit unions in particular should bear their share of the tax burden, and we have directed our recommendations to that.

THE CHAIRMAN: Do you consider it is equally as easy to measure their income as it is taxpayers such as yourselves?

MR. HOWARTH: Not necessarily as easy, Mr. Chairman. We would expect there would be problems in doing so, but if we could make a general suggestion of an approach that might be made, we feel that one area that could be considered for taxation as an introductory step might be their retained earnings; earnings in the sense of

the excess of their income over their expenses of operation. However, if you are using the word "easy," Mr. Chairman, in the sense of accounting?

THE CHAIRMAN: Yes.

MR. HOWARTH: We appreciate there would be problems. Probably it would involve a considerable study of their present accounting operations, but we do not believe this would be an insurmountable obstacle. We feel this is an operation involving dollars and cents, and if the will was there to apply taxation, this could be done, but not without proper study.

THE CHAIRMAN: So long as they lend money to their own members could they not reduce or, in fact, eliminate tax by reducing their interest charges?

MR. HOWARTH: In the sense of reducing the cost of their operation down to the income that they would derive? I think they could do that just as much as any other organization could if it wished to do so. There could be nothing that I could see to prevent it. Perhaps Mr. Jarmain would speak to that.

MR. JARMAIN: I am not an expert on credit unions; this I should confess to start with. It does seem to us that one of the tests of what we have chosen to call commercialism which we feel has arisen in the credit union organizations on this continent has been the retention of earnings, which, as I understand it, is quite contrary to the original intention of the credit union movement, which was to provide mutuality of service in a cohesive group which they could not provide individually.

Measuring their income and measuring their

expense really is not technically difficult. I agree with you that if they choose to operate on a break-even basis, and assuming for the moment that they had reserves for possible losses in that group, I think they would be confined to what was intended originally.

The position, we feel, is when they began to borrow from banks and they began to borrow from other sources, including short-term money markets, they have gone beyond the original intention, and, in fact, are
3 subsidized by tax-paid dollars in competition with organizations like our own and chartered banks.

THE CHAIRMAN: It would seem to me, you see, that they could operate quite satisfactorily in such a manner so as to break even rather than make a profit. The law requires that they establish certain reserves and I would have thought that since the law acknowledges those reserves, they must be recognized as deductable from their income and treated as expenses. If that is so, we are, of course, curious as to whether income tax is something that might be properly applied to an organization which, because it is not at arm's length really with its borrowers, cannot operate quite satisfactorily without, in fact, making a profit. If that is so, there is not much merit to recommending taxation of that kind.

COMMISSIONER WALLS: I note in your introduction more than 90% of credit extended by your members is for business, for machinery and equipment purchases.

MR. HOWARTH: I do not think you have the context of that properly; not more than 90% of the credit we extend is for business, but our members extend over 90%.

COMMISSIONER WALLS: I understand that, although I may have stated it wrongly. Surely that is a branch of industry or lending in which you have no competition whatsoever from the credit unions.

MR. HOWARTH: We have very little competition from the credit unions, to my knowledge, in that area, but I believe there have been occasions of commercial lending. I did hear of an example of a credit union in Hamilton financing a bowling alley. You are quite right. This area of financing of equipment for business and industry is not one in which we come into contact or competition with the credit unions. The competition we have with credit unions is in the consumer.

COMMISSIONER WALLS: In the consumer finance?

MR. HOWARTH: Yes.

COMMISSIONER WALLS: In consumer finance how do your interest rates compare with the credit unions'?

MR. HOWARTH: Well, the credit union rate is 1% per month of the outstanding balance, which is 12% per annum rate.

COMMISSIONER WALLS: Right.

MR. HOWARTH: The rates that our companies charge would vary depending upon the type of receivable that was being financed. New cars today, for example - the rate would range from, I believe, somewhere in the neighbourhood of 11½% up to 15%. Something across that range. If you get into used cars or other small balance items where you have got to recover a certain number of dollars, the rates will go up to 20, to 25 per cent, depending on the particular type of transaction.

COMMISSIONER WALLS: So that really to the small man, provided that the co-operative unions stay servicing the small man, they are giving him overall, generally, a lower interest rate than the normal finance companies are giving? I mean overall. I agree on some items you are giving $11\frac{1}{2}$, but overall they are giving a lower interest rate.

MR. HOWARTH: I think if you use the term "overall" I would have to say yes to that. May I just add one point here that sometimes is lost sight of? While the credit union rate is 1% per month, which is 12% per annum, it is also considered good credit union practice to encourage members to leave their funds on deposit if they have funds on deposit.

If I can give you an example: if a man has, say, $100 on deposit with a credit union, and say he needs $200 for some purpose, he can go to his credit union and arrange for a loan of, say, $200, or he might withdraw $95 and leave $5 on deposit and borrow the rest.

COMMISSIONER WALLS: Yes.

MR. HOWARTH: Now, it is considered good credit union practice, and I believe in the interests of keeping savings intact you can make a case for it there to encourage that man to leave savings on deposit and make a loan for the balance, which he will repay at proper intervals.

COMMISSIONER WALLS: After all, is that not what the life insurance companies also do? Rather than cash your policy in, you borrow from it and retain the policy.

MR. HOWARTH: Oh, well, I think there is a

slight difference there. May I finish my illustration?

COMMISSIONER WALLS: Yes.

MR. HOWARTH: If, as I believe frequently occurs, the man borrows the full amount of his needs, leaving his money on deposit; in my example, where he would borrow $200, and leaves $100 on deposit, the net investment of the credit union as an institution is only $100, and that has a very definite effect on the rate.

Now, I am not discussing the desirability of the transaction, but you raised the question of rates, so that the effective rate that the credit union would earn in such a transaction would be 23 or 24 or 25 per cent. This, I believe, from the evidence I have seen, is considered good credit union practice.

COMMISSIONER WALLS: I would not know about that, but I do know from their bylaws there is nothing to stop a man withdrawing his $100.

MR. HOWARTH: Absolutely nothing.

COMMISSIONER WALLS: We can only go by the bylaws rather than on hearsay, can't we?

MR. HOWARTH: This is not hearsay.

COMMISSIONER WALLS: I see. Is it not right that the credit unions perform another service that your finance companies do not, and that is one of encouraging savings amongst small people?

MR. HOWARTH: Oh, definitely.

COMMISSIONER WALLS: You are quite prepared to loan ---

MR. HOWARTH: We give them full marks for that in our brief. Within the confines of the small group, we

feel the credit unions are a positive and, in many respects, a useful part of our society. Personally, I have on two occasions been a member of a credit union in two previous employments I had, and they were both industry, and I believe in every respect they fulfilled the original purpose of the credit union.

COMMISSIONER WALLS: Thank you. That is all.

COMMISSIONER BEAUVAIS: Would you consider that the Caisses Populaires in Quebec were credit unions?

MR. HOWARTH: In the sense of our brief, yes.

COMMISSIONER BEAUVAIS: Because I think that is a quite different organization. Do you not think so?

MR. HOWARTH: Well, I believe its basis is parochial, but to the extent of retention of earnings and to the extent of borrowing funds from outside sources, I do not see that it differs in any way.

COMMISSIONER BEAUVAIS: I think, though, the equity or the reserves do not belong to the members. If there is a winding-up, for instance, all the reserves except capital stock will be given to charitable institutions or education.

MR. HOWARTH: I was not aware of that, Mr. Beauvais.

COMMISSIONER BEAUVAIS: As directed by the Lieutenant-Governor in Council of the province, so that they have no say in the distribution of their reserves. The only income that the members will receive is the dividend, and the dividend is from 4 to 5 per cent. Moreover, the interest rate is not more than 6%. There is also an insurance to cover the loan. Therefore, it seems to me

that we should make a difference between the Caisses Populaires in the Province of Quebec and the credit union.

MR. HOWARTH: Well, with respect, Mr. Beauvais, I am not familiar with those particular rates that you are mentioning there, but we would still argue that if they are creating earnings in their operation, that they should bear their share of the tax burden. I was not aware of this - you say if they were winding up, in other words, the net resources would not return to the members of the organization?

COMMISSIONER BEAUVAIS: That is right.

MR. HOWARTH: I did not know that. Even so, dealing strictly with the question of profitability and tax, we would not vary our recommendation there.

COMMISSIONER BEAUVAIS: Yes, but for the record I would like to say there is quite a difference, and they should not be considered as a credit union in the sense that credit unions are used in the brief here.

COMMISSIONER PERRY: Mr. Howarth, you will agree that a key point here is one which you emphasize throughout your brief, and that turns on the statement that credit unions have become commercial in character. You mention this several times. This is a rather subtle sort of concept. We had a credit union before us yesterday, and I asked them if they would continue to argue that the character of their movement had not changed if eventually they were doing all the financial business in the country,
4 and they said they would continue to argue that; that the basic concept of their movement had not changed even if they ever reached the point where they had all the deposits

and were making all the loans.

MR. HOWARTH: Did you wish me to comment on that?

COMMISSIONER PERRY: I just wondered what are the indicia here. It is theoretically conceivable that size is not an indicia; that eventually credit unions could take over the whole financial system, always operating within your statement of what is the basic function of a credit union.

MR. HOWARTH: One thing I am amused to hear: how they have answered that question. Some of their own leaders in the United States have been very self-critical about the development that has occurred in recent years.

B/MC/ss

We would look at it this way: One criterion might be the original common bond concept of borrowing from members, or at least having the savings of members available for lending to members when they have a provident or productive purpose.

When a credit union goes to the point where it will borrow funds either from the Central organization or a bank to carry on operation within that credit union of lending, I cannot see any distinction between what our industry does or the banks or small loan companies.

The original concept of the credit union of the common bond was, I believe from my reading of their history, that the group itself was self-sustaining and there was a sense of cooperation, of brotherhood within its own membership. We cannot see that as being maintained when borrowings take place from outside the particular membership. That is one example.

COMMISSIONER PERRY: I had written this down from a previous statement you made. It seems a valid point of thought, but their own consolidated balance sheet shows very little borrowing from outside sources.

THE CHAIRMAN: Mr. Howarth includes their central organization as well as outside sources.

MR. HOWARTH: From our way of thinking this has all the earmarks of a branch banking system. To take their example, if all the financing of the country became the business of the credit unions and they say that would not have departed from their original concept --- I cannot accept that as a valid argument.

COMMISSIONER PERRY: It is difficult to accept.

There must be some reasons for not accepting it. I am not clear what they are.

MR. HOWARTH: We don't see any particular distinction between the operation of a credit union that uses resources outside its membership from that of any commercial organization in the tax-paying groups.

COMMISSIONER PERRY: I think this is verging on a valid point. Could you think of anything else? That is one of the indicia of commercialism.

MR. HOWARTH: One example would be the flood of advertising that is engaged in today by credit unions in certain areas. When a credit union in Hamilton will take T.V. time to advertise for general membership, we feel this has the earmarks of a commercial organization. You see, Mr. Perry, when your bonded membership is residents it is a pretty flexible thing. There are credit unions active today that are residential rather than industrial or church or fraternal organizations.

COMMISSIONER PERRY: I asked for some details on this. They mentioned that the largest industrial credit union would be in Hamilton in the steel company, and this would have 10,000 members and if they did do any advertising it was not to attract membership at large, but to draw to the attention of people who were eligible the fact that there was a credit union. This was a fairly carefully thought out statement that they did not advertise for general membership.

THE CHAIRMAN: There was one further restriction imposed, namely, that residential unions could not be established in towns which had a population in excess of

6,000 people. They could not secure a charter.

MR. HOWARTH: Would this be a Provincial credit union group you were speaking to?

THE CHAIRMAN: Yes.

MR. HOWARTH: I don't think this is general in all provinces.

COMMISSIONER PERRY: This was the Ontario group. They did mention community credit unions, but they are in small places like Dundas and Dundalk. We will have to continue this.

MR. HOWARTH: If I could summarize our thinking on this and say that we have to contend with competition from credit unions in our industry as other lending institutions do, and we would sincerely believe that the mechanics of taxation could be worked out, if this was decided as a proper course. You might be interested in the comment that was made, if I might make it here, by the American Bankers' Magazine in its November issue of last year on this general point of taxation of credit unions.

We have suggested that the credit unions' profits be taxed. The American Banker pointed out that equity could be achieved if in addition to allowing exemption for credit unions in this tax area similar exemptions were made available to other institutions such as the American banks and finance companies and so on. They say that competition in this area is so keen that benefits would percolate to the consumer, and this would be a general benefit to the borrowing consumer.

This, to me, was interesting. Somebody thought

of it going the other way. Our recommendation is in view of the heavy burdens that Government has to meet at the Federal level that the credit unions be required to pay their share of the tax.

THE CHAIRMAN: Thank you. As you are undoubtedly aware, we have heard several suggestions to the effect that corporation tax be done away with. I suppose that would very nicely take care of this problem!

COMMISSIONER GRANT: Would you give us a little further information as to the composition of the Council of Sales Finance Companies and what are the qualifications for membership in the Council?

MR. HOWARTH: The Council, Mr. Grant, was formed in 1957, a fairly recent association as associations go. Its membership consists of companies who are, using our phraseology, independent sales finance companies and companies who compete for the receivable paper that is available in the general market. This would exclude from membership such companies as, say, Simpsons-Sears Acceptance or Eatons Acceptance or acceptance companies geared to a particular dealership or particular manufacturer. Our companies compete for the general availability of acceptance paper, conditional sales contracts. Our membership does not include the so-called small loan companies, even though some of our companies do have subsidiaries in this field. Our association represents the companies conducting the financing of conditional sales contracts.

COMMISSIONER GRANT: Do you lay down any regulations within the Council as to the method for raising money by your membership?

2 MR. HOWARTH: No, we just have the general bylaws on ethical behaviour, not specific as to raising of money.

COMMISSIONER GRANT: You have never had occasion to reject a membership because you objected to its way of raising money?

MR. HOWARTH: No.

COMMISSIONER GRANT: Have you lost any membership since you began?

MR. HOWARTH: Yes. We started off in 1957 with eight companies and we now have 39. I think that is the figure. We have lost the odd small company which is either a one or two-branch operation, usually where there was a change of management or something of that nature.

I did not expect you to raise that point, but I am glad to say that this year we have renewed 100% of our membership.

COMMISSIONER GRANT: Is your membership under some sort of surveillance by your Council?

MR. HOWARTH: If I could make a distinction here, I was formerly associated with the Canadian Institute of Chartered Accountants, which is the central body for the ten provincial groups. A professional organization like the Chartered Accountants or the Bar or Medicine has disciplinary powers. It does have the right to grant or withdraw a man's qualification, so you can see in a professional body of that kind you have teeth. You can say to a man if he does not toe the line he will not keep his professional standing. You have something to apply which will make him toe the mark.

Ours is not quite like that. We are, in common with most industrial groups, just a voluntary organization. You can join or not join as you see fit. We hope that by responsible leadership of the industry it will come to mean a mark of prestige to belong to and support its operations and its purposes. There would be no penalty that we could apply other than dismissal. We have no other means of applying a penalty to, say, either of my colleagues' companies or any company in the organization.

We have, I think, grown reasonably soundly over the years. We have now about forty members. Our growth has been fairly steady and we have sustained most of our membership. We have no way, other than I would say, the not unimportant factor of mutual respect and recognition amongst the membership companies, we have no penalties we could apply.

COMMISSIONER GRANT: My questions are prompted by the fact that I seem to recognize in your list of members the names of some companies that have been in the news lately as to their method of raising money and mention has been made as to whether or not their advertising and their solicitation conforms to Provincial laws.

MR. HOWARTH: Yes. There has been recently a law introduced in Ontario as an amendment to the Securities Act, a new Deposit Taking Act, which will bring this type of operation under closer control. This was at the last session of the House these changes were introduced. They are regulations which I believe will be adopted, or similar ones, in other provinces throughout the country.

COMMISSIONER GRANT: It seems to me that they have managed to work within the law in some provinces, because of the fact that they advertise their debentures or their notes as being available only to their own shareholders or their own members and for less than one year. In that way they are not bound by the Security Acts of the provinces which require registration for the sale of debentures.

MR. HOWARTH: Is this a recent development, this business of being shareholders?

COMMISSIONER GRANT: Within the last six months.

MR. JARMAIN: Perhaps I might help on this. I think you have two separate things here. As far as I am aware under the Security Law in each province a promissory note which matures in more than a year is exempt from prospectus and registration requirements. The sale of any kind of security running more than a year may be exempt if it is directed only to present note-holders or other people who are already investors. I think this is the transaction you are referring to .

COMMISSIONER GRANT: Yes.

MR. JARMAIN: There was an issue of longer term notes. As far as I am aware that was perfectly proper within Ontario law as it was constituted then, and as it stands now.

COMMISSIONER GRANT: The type of the security offered and the manner in which your membership is raising its money would, I should think, have some bearing on your suggestion that the reserve be set up out of earnings and before taxes and along the lines which is now

permitted for mortgage reserves. I am referring to mortgage reserves. My purpose in asking these questions is to find out the risk involved to the public when money is raised, say, through deposits or through short-term notes.

MR. JARMAIN: If I might quote one of the gentlemen of the press, who I think is here now, who said that the interest rate paid is a fair measure of that risk.

COMMISSIONER GRANT: That depends on the success of the company, I suppose. If the company is making money, then it could meet its obligations. If it is not making money, it would not be able to meet its obligations.

THE CHAIRMAN: The second point that you refer to in your submission concerns the Industrial Development Bank. I am really surprised to find the Industrial Development Bank is offering strong competition. I had no idea that was in fact the case. I was a little surprised at your suggestion that the way to level this out is by using the Tax Act and denying a deduction in respect of their interest. It occurred to me that perhaps a not unreasonable alternative might be to impose income tax on the Industrial Development Bank. Certain Crown companies are taxed. This one, I believe, is not. I suppose under those circumstances its costs would then become comparable to those of ordinary commercial organizations.

MR. HOWARTH: It would bring them closer together, Mr. Chairman. There is the very important point that the funds of the Industrial Development Bank are made available

from the Bank of Canada at a rate --- I don't think it is public --- I am given to understand it is about $\frac{1}{2}$ of 1% above the Bank of Canada rate. While you would narrow 3 the gap between the cost of operation of the I.D.B. and, say, companies doing comparable business in our industry it would not completely close it. There is a further factor here. Maybe we should have enlarged upon it in the brief. That is our suggestion that from the point of view of the fiscus this would bring revenue in if you tax the I.D.B. as distinct from borrowers by removing the deduction from tax.

ET/dpw We are concerned as an industry that customers or borrowers who receive I.D.B. financing, which they do at a preferred rate in comparison to commercial rates, be prepared or encouraged to stand on their own feet as soon as possible. In other words, we do not want them to become I.D.B. customers for financing on a perennial basis, and we are alarmed and concerned that an enterprise which uses I.D.B. financing at a particular stage of its development may continue to re-finance and re-finance and be removed entirely from the normal competitive commercial area.

The point of our recommendation is that the deduction from taxable income would only have bearing on this particular enterprise as it became profitable, at which time it would be better able to stand on its own feet, and on a financial basis, while this would not necessarily be a large area of revenue to the Government, it would have, we believe, a sound effect on the operation

2 of this enterprise. Your counter-suggestion there for taxing I.D.B. is one that I do not think our industry would quarrel with at all, but we do not believe it would have this effect.

THE CHAIRMAN: If one disallowed the tax deduction on successful borrowers from I.D.B., the rate, instead of being whatever it is, we will say 6%, would become virtually 12% and an uneconomic rate for any borrower.

MR. HOWARTH: You state from six to twelve?

THE CHAIRMAN: If it was disallowed for tax purposes.

MR. HOWARTH: Is that an envisaged 50% rate?

I will put it this way: anyone who can sustain a 50% tax rate should not pay ---

THE CHAIRMAN: I prefaced my remarks with "successful borrower." I said a successful borrower. I did not mean success in achieving the loan. I meant having obtained the loan, success in its operations. If it were successful in its operations to the extent of making good profit, which is obviously the purpose of the loan, and it needs to make a good profit to pay off the loan and become a solvent company, it would place a considerable strain on its ability to achieve this because it would then amount to roughly 12%. One could find few borrowers who could pay that kind of money and have enough left over to be of value to the enterprise, I would think.

MR. HOWARTH: I do not think that I could quite accept the spread that you suggest there in terms of the success. I do not believe it could be reached that rapidly. At least that would be my feeling on it.

THE CHAIRMAN: You mean the tax rate would not be 50%?

MR. HOWARTH: I would think that would be an extreme case.

THE CHAIRMAN: I am using the marginal rate, but I think that is fair in the circumstances. You may be correct. I would have thought that if it is a worthwhile concern, a 50% rate would hit $35,000 in profits, and that is not such a tremendous attainment.

COMMISSIONER GRANT: The I.D.B., once a loan is made, they take as security for that loan such immovable

assets as the company might have by way of mortgages, and such movable assets as the company may be able to offer. Do you know the length of time that the average I.D.B. loan would be? The length of time for repayment?

MR. HOWARTH: I will consult my colleagues on this. Generally, the I.D.B. is prepared to lend for longer periods than our industry.

COMMISSIONER GRANT: That is what I thought.

MR. HOWARTH: I believe five and ten-year periods.

COMMISSIONER GRANT: Now, your purpose in bringing the I.D.B. into your brief is to bring out the fact that it is unfair competition to the members of your particular Council?

MR. HOWARTH: That is correct.

COMMISSIONER GRANT: Well, just on interest rate alone, do you think a borrower for a commercial enterprise which has now been taken care of within the objects of I.D.B. could go to a finance company such as any member of your Council and pay the higher interest rate of, say, 12%, which would be minimum, as compared to the bank rate?

3 MR. HOWARTH: Would you care to comment on that?

MR. JARMAIN: I do not know the source of your 12% minimum on this class of business, but we would love to get 12%.

COMMISSIONER GRANT: Perhaps you can enlighten me on that. Do you take loans for less than 12%?

MR. JARMAIN: On the kind of business that the Industrial Development Bank competes on, 12% would be

higher than any rate anyone gets today. Nine to eleven per cent would be the range. The tendency is to get below nine.

COMMISSIONER GRANT: Some of your members will lend below nine per cent?

MR. JARMAIN: Mr. Doig's company and mine do regularly.

MR. HOWARTH: On this class of business.

COMMISSIONER GRANT: Over what period of time?

MR. DOIG: As high as twelve years. Twelve and fifteen years.

COMMISSIONER GRANT: Are these national companies to which you refer, companies which have offices pretty well coast to coast?

MR. HOWARTH: Mr. Doig's company is the largest one in Canada, sir.

COMMISSIONER GRANT: In your experience, Mr. Doig, did you have occasion to finance commercial loans of the type which I.D.B. are now financing before I.D.B. came into existence?

MR. DOIG: I cannot recall, Mr. Grant, but I would guess that we did.

MR. HOWARTH: Could I add something there, Mr. Grant? One of the ways in which the I.D.B. competition was brought home to us most strenuously over a period from about early 1960 through until last Fall was in the pay-out of business that we had on our books by I.D.B. This is where the competition was really most strenuous and severe.

In terms of totals, it was in millions of

dollars, and in many cases there would be a particular piece of financing, say, which had originally been loaned; say, $300,000 that had been paid down to $150,000, and then the pay-out would come from I.D.B. So in terms of the type of business, we were losing customers to I.D.B. which had, in many cases, maybe over a period of 8 or 10 years, been using the services of our industry.

COMMISSIONER GRANT: Of course, it would be asking entirely too much if you were to give us instances of why they re-financed with I.D.B. rather than re-financed with the company they were doing business with.

MR. HOWARTH: I think we made a very careful analysis of a number of these cases, and we have case histories if your Commission would like to have them. In almost every case the deciding factor was rate. In other words, we just could not compete with the I.D.B. rate.

There may have been the odd case where the term, which you introduced a little earlier, had some effect, but not from our own experience, going back to our field people who had put the business on the books and so on; the rate was the deciding factor. Mr. Jarmain has mentioned 9 to 11 per cent.

MR. JARMAIN: Yes, that is the common rate.

MR. HOWARTH: It is a very competitive area, but the re-financing through I.D.B. in the cases where we felt there was a loss to us, a competitive loss, was on the factor of rate.

COMMISSIONER WALLS: Is it not a fact when I.D.B. went into existence it was not to supplement the

existing financial institutions, but was to give a form of credit that the banks at the time were restricting ~~credit~~ and were unable to offer to industry? In other words, it was to give long-term loans, and at that time banks were only interested in short-term loans, and your own organizations at that time were not giving long-term loans.

MR. HOWARTH: Well, the preamble of the I.D.B. sets out many conditions for its lending. I think our basic position on that, Mr. Walls, would be that I.D.B. should only step into the picture when the particular accommodation is not available in the normal lending area wherever that may be. We feel there has been a competitive development here, a rather aggressive development, by I.D.B., which has brought it into a competitive position with us rather than supplementary.

COMMISSIONER WALLS: You do not think I.D.B. could say the reverse; they went into this business when no one else was prepared to give this credit of 10 to 15 years and therefore in recent years they have now been competed with by both yourselves and the banks going into long-term credit?

MR. HOWARTH: If they said that I think we would challenge it to some extent.

COMMISSIONER WALLS: The next question I would like to ask you is this: you only mention I.D.B. What about the other government lending institutions, that operate on the same basis, who borrow from the Minister of Finance for half a per cent lower than what they charge on the loan, or 1% less? I am thinking particularly of the Farm Credit

Corporation which is lending today over ninety million dollars a year. How are you going to draw a line of demarcation between them, because I am quite sure you would not want to compete and go into agricultural financing, or would you?

4 MR. HOWARTH: We have been in it for 35 or 40 years.

COMMISSIONER WALLS: Yes, but running to the types of loans that they are granting?

MR. HOWARTH: Well, our industry has been lending or financing agricultural equipment and machinery for many, many years.

COMMISSIONER WALLS: At 5%?

MR. HOWARTH: We cannot finance at this rate. This is a government-guaranteed rate. In our consideration of this, for instance, we question today whether the guarantee is necessary to the banks in many of these instances, but we certainly are in this field of financing.

COMMISSIONER WALLS: If so, I would be interested to know why you have picked on I.D.B. and have not picked on other government lending institutions, that is all.

MR. HOWARTH: We feel it was an oversight after consultation.

COMMISSIONER BEAUVAIS: Mr. Howarth, I have a question on this problem. If a borrower cannot obtain a loan from you or from the bank, and can obtain this loan from I.D.B., according to your suggestion he will be penalized because his interest will not be allowable for income tax purposes.

MR. HOWARTH: I am not sure if I have the sense

of your question, Mr. Beauvais.

COMMISSIONER BEAUVAIS: Well, a borrower will be refused by a bank or your institution.

MR. HOWARTH: Yes.

COMMISSIONER BEAUVAIS: And will be accepted ---

MR. HOWARTH: Would be accepted by I.D.B.?

COMMISSIONER BEAUVAIS: Yes. Then, by the mere fact of your suggestion, he would be penalized because his interest would not be allowed for income tax purposes.

MR. HOWARTH: I think our answer to that would be: if he is refused by the banks and by our industry and must find his financial investment from I.D.B., it is most unlikely that his balance sheet and profit and loss statement is going to be in a tax-paying position. You see, here our thought is this is only significant as he moves into the area where he is taxable and able to meet his obligations. It was not our thought that it would be a penalty.

We feel it would be a proper bringing of him into an area of meeting his share of the overall tax burden as his business became profitable. In other words, if, in the year in which he obtains this financing from I.D.B., which is not available from normal commercial lenders, this would only have a bearing if he is in a position of profit for his operation.

COMMISSIONER BEAUVAIS: You infer that if a man is refused by the banks and your companies, then he should not get a loan from I.D.B.

MR. HOWARTH: No.

COMMISSIONER BEAUVAIS: Because when I.D.B.

started, and I had some experience at the beginning, we could obtain a loan for a client that was refused by a bank and other credit institutions, and I think that was the idea of creating I.D.B. at the beginning.

MR. JARMAIN: It might help if I try to recall how this came to be in the brief. I shall confess I was the actual author of the words. I.D.B. represents very severe competition for our companies. We feel it is subsidized by our tax dollars and other people's tax dollars no matter how they are accounted for.

Our first thought was exactly what your Chairman has suggested, that we would recommend that I.D.B. be subjected to income tax. However, there was a number of people around that table who felt I.D.B. served or could serve the purposes for which it was intended. It is our feeling, as we have said in the brief, it has gone way beyond what was intended.

Whether the device we have suggested would actually be workable or not we have no statistics to prove, but our thought was that this was a sort of thin edge of the wedge, if you like, from the point of view of gradually increasing the burden of the interest rate of an enterprise which I.D.B. should and was set up to support.

As the profitability of that enterprise increases then the burden of taxation would increase with it. There is no intention on anybody's part to penalize anybody here, and I hope the brief does not give that impression. It was not written with that in mind.

COMMISSIONER BEAUVAIS: If the borrower has to

pay twice the interest rate or less than twice if he is in the 23% bracket, surely he is penalized. It is not his fault that I.D.B. is not subject to income tax.

MR. JARMAIN: I agree with you, sir. If he were earning enough profit, and you do not have to earn very much, as Mr. Carter has pointed out, to be taxable at the top rate, but we have to remember our income tax law does provide for a period of six years over which profits and losses can be equated with some ease.

I think we should also recognize that an organization which is profitable probably would not be refused either by us or by a bank if we were given a chance to talk to him before I.D.B. talked to him.

COMMISSIONER BEAUVAIS: Then we have to assume that I.D.B. should disappear?

MR. JARMAIN: No, sir, we don't think so. That is why we went at it this way. If we were to adopt
5 Mr. Carter's suggestion, I think it would disappear. I do not think it could compete with us.

THE CHAIRMAN: I am inclined to think that might be the more natural result.

MR. HOWARTH: Up until about two-and-a-half years ago there was no thought in our industry's mind of ever cramping I.D.B.'s style or objecting to the nature of financing it was doing. We believe it plays a very necessary part and can play a very necessary part in the economy, and to be quite frank, there are cases where people have come to us that we have not been able to accommodate and that we have been pleased could go to I.D.B. There is no question about that.

It is the expansion that is of concern to us. We believe that there has always been a necessary role, and that this would continue for I.D.B., but we believe it has gone beyond its intention and what is best for the economy.

THE CHAIRMAN: The main burst of expansion has occurred in the last year, has it?

MR. HOWARTH: No, sir. I would say from early 1960 on.

COMMISSIONER GRANT: Would you give any reason in your mind as to why that expansion has taken place?

MR. HOWARTH: I can give you my personal feeling about that. I think that expansion was sparked by the desire of government to invigorate the economy. They saw this as an expanded I.D.B. operation, as one that would be providing employment and use of our resources. One thing we would be critical of, and I do not know that we mention this in our brief, but we did when we discussed it with the Royal Commission on Banking and Finance, and that is that I.D.B.'s figures of outstandings which are a gauge of their contribution to the economy never could - never did, and probably would have difficulty in doing so - never showed to what extent this amount was a duplication or replacement of financing that would have been provided by the private enterprise sector.

To answer your question I believe this was a deliberate attempt, and one that we could not quarrel with as far as the goal was concerned, of sparking the economy and providing some employment as we went along.

COMMISSIONER GRANT: I was wondering if the

expansion was due to the fact that they are less particular in their type of risks now than they were when they started out.

MR. HOWARTH: It could be, in part. I might add, sir, the regulations under which they operate were greatly expanded or it was made possible for them to undertake a much wider group of loans and financing than they were previously able to do.

COMMISSIONER GRANT: They have become more relaxed in their requirements for security and risk, but then that expansion might not be at the expense of competing organizations.

MR. JARMAIN: There is no indication, sir, that they are really extending credit wildly - I am not trying to put words in your mouth - but I am exaggerating deliberately. There is no indication that they are extending credit in what you would call a wild fashion. Their losses so far do not indicate they are.

MR. HOWARTH: Our main complaint is that they have been extending credit at a more attractive rate to many customers that would have been placed on our books.

COMMISSIONER GRANT: When you say a more attractive rate, do you mean they have lowered their rate?

MR. HOWARTH: No, sir. I believe there was a slight increase a while back, but their rate is a rate that is not competitive. We cannot compete with it, of course. I believe they have been anywhere from around 2% lower.

MR. JARMAIN: Their rate runs $6\frac{1}{2}$ to 7 per cent.

MR. HOWARTH: And ours would be 9 to 11.

THE CHAIRMAN: I assume you will carry your complaint elsewhere than here?

MR. HOWARTH: We have been carrying it in many directions.

THE CHAIRMAN: Then, the third point which you put before us concerns reserve for losses on receivables. This reserve for losses is essentially a matter of accountancy. There is a bulletin from the Canadian Institute of Chartered Accountants relating to reserves, and you will recall the content of this probably better than I will, but it seems to me it restricts reserves to the accounts outstanding at the end of the year; it does not recommend cyclical reserves as one might refer to anything extending over a period of time except in the case of banks, or does it go to all financial institutions?

MR. HOWARTH: I wish I were more familiar, and I bow my head in shame that I am not.

THE CHAIRMAN: I take it that your concern is with reserves sufficient not just for the moment but to take care of losses over a period of time; is that correct?

MR. HOWARTH: Our concern is that the approach to the reserves on an annual basis is not realistic in terms of the type of receivables that we hold. On this particular area of our brief I would like Mr. Doig and Mr. Jarmain to make their comments.

THE CHAIRMAN: One more question before they do. I assume that the assessors, generally speaking, admit a sufficient reserve to take care of accounts then outstanding against which the reserve is provided, but not to go into the future? Am I correct in that

general assumption?

MR. DOIG: To some extent. In view of the fact that we have not had our reserves touched by the assessors in the last eight or nine years, that would be so, but there is some indication that has been given to us that they feel our reserves are too high and they are going to base their reserves in future on the previous year's losses which we feel is sort of a threat hanging over our head, which is wrong in principle.

COMMISSIONER WALLS: You feel it should be a percentage of the accounts receivable?

MR. DOIG: I think you have got to have a basic reserve based on that, but I do not think that is the whole answer because your portfolio could deteriorate very considerably over a year's period, and the established percentage would not be sufficient. I think it would be more likely to establish a percentage on receivables below which your reserves should not be questioned, but if you found it necessary to establish a reserve above that percentage, then you have got to justify it by individual accounts.

COMMISSIONER GRANT: In the question of establishing reserves, and having regard to the suggestion that it might be along the line that is permitted for mortgage companies - and if I am wrong here, you correct me - in the case of mortgage companies there is a restriction as to the amount of the loan. Now, there is no restriction, I would take it, in the case of the finance companies. That depends upon their own discretion?

MR. DOIG: I think, perhaps, Mr. Grant, we are

talking of two different things; the consumer figures on which we would expect a certain percentage of loss reserve, and when we get into the other area which we in our company call capital funds financing which is similar to the I.D.B. type, most of that financing is covered by mortgages, secured by mortgages, and we think the reserve in that area should come close to the mortgage reserves, but not the other.

COMMISSIONER GRANT: In taking those mortgages, are they subject to the requirements of the Loan Companies' Act in the provinces?

MR. DOIG: Yes, they would be. Perhaps I had better ask just what restrictions are you referring to?

COMMISSIONER GRANT: For instance, there are some provinces that say a mortgage shall not exceed two-thirds of the appraised market value of the property.

MR. DOIG: That is trust companies.

COMMISSIONER GRANT: Well, it could be a loan company.

MR. DOIG: No, our mortgages will exceed 66.2/3%.

COMMISSIONER GRANT: I was asking as to whether or not you are bound by the requirements of the Loan Companies' Act in a province or the Trust Companies' Act in the province.

MR. DOIG: No; I would say no.

COMMISSIONER GRANT: So that the percentage of risk is a matter for your own discretion?

MR. DOIG: Right, and because the rate is higher the risk could be assumed to be greater.

THE CHAIRMAN: We have no more questions, Mr.

Howarth. Is there anything else you would like to say to us?

MR. JARMAIN: One thought occurred to me, and this is going back to I.D.B. There is one word I ought to have recalled to you when we were talking about it, if I can find it. Our recommendation is that in our opinion the rate at which I.D.B. lending takes place should impose a reasonable burden upon the borrower.
6 That was carefully phrased to indicate we were not suggesting that the current rate or any other rate necessarily should be maintained, and this is part and parcel of our recommendation. I felt I should draw that to your attention.

THE CHAIRMAN: Those words are already underlined in my copy here.

MR. JARMAIN: I quote it only to reinforce the statement I made. We were very conscious of a place for I.D.B., and a very important one, in the economy.

THE CHAIRMAN: We very much appreciate your attendance here this morning and your giving us this interesting and most useful submission. Thank you very much indeed, gentlemen.

MR. HOWARTH: Thank you, Mr. Chairman.

THE CHAIRMAN: We will stand over, Mr. Secretary, for ten minutes.

--- Short Recess

IC/ss

SUBMISSION OF

THE GOVERNORS OF THE UNIVERSITY OF TORONTO

APPEARANCES:

Mr. Hamilton Cassels, Q.C.
Mr. A. E. Charlton

THE CHAIRMAN: Mr. Secretary, are you now ready?

THE SECRETARY: All ready, Mr. Chairman.

THE CHAIRMAN: Will you introduce our visitors?

THE SECRETARY: You now have a brief before you presented on behalf of the Governors of the University of Toronto by Mr. Hamilton Cassels, Q.C. Mr. Cassels will speak to the brief and he has associated with him this morning Mr. A. E. Charlton.

I would like to enter this into the record as Exhibit 77.

---EXHIBIT NO. 77: Submission of the Governors of the University of Toronto.

THE CHAIRMAN: Mr. Cassels, we are not only pleased to greet you personally, but also as appearing on behalf of the Governors of the University of Toronto who are landlords in this very excellent premises. I am happy to acknowledge how much we are indebted to them on that score.

We have received your submission which concerns the matter of Estate Tax. There is no need to read it to us, we have already read it. I would be grateful if you would say a few words to us. Stand if you wish, but we are perfectly happy if you care to remain seated.

MR. CASSELS: Mr. Chairman, madame, gentlemen, I am afraid I am a little bit apt to become intemperate in language when I talk about this particular matter, because I think it is not stretching it to say that the present provisions --- it is a narrow point, as you may have seen from the brief --- but I think it really is an iniquitous situation.

I am assuming that you have all read the brief. It is not only departing from the wishes of the testator in each case but it is putting the trustees in a position where they really are asked to commit what is tantamount to a breach of trust.

The narrow point is simply this: In a great many estates nowadays, to avoid double taxation, the testator leaves a life interest in his estate to his widow, or members of his family, with a provision that in the event of need the trustees may encroach on capital, with the remainder or the residue going over to usually the younger generation. That is the typical form of will that is now, I think it is fair to say, most common.

Now, because of the fact that this provision for encroachment on capital is inserted in the will, the Federal Government is treating that, if it is unlimited power of encroachment, as if it were an outright gift to the life tenant. That means, in the case of charity, and it is only in the case of charities that I am concerned with it, in the case of a charity it means they are deprived very often of a substantial amount, because what should have gone to them is going in taxes to the life tenant or on the life tenant's interest.

In using the expression "charity" you are all no doubt aware of the fact that it is the same old definition that goes back tothe Statute of Elizabeth, charity in a general sense being considered as the relief of poverty or gifts for the advancement of religion or education or other purposes for the benefit of the public not included in those terms.

Now, the first intent of the testator is usually to provide first for his own family and the gift to charity is after provision has been made for his family, the typical case being, of course, the widow. He gives her probably the interest for life on the residue of his estate, but he cannot look into the future and be sure that there won't be some emergency which will mean that the income will be insufficient. He puts this provision in that his trustees may encroach on capital if they consider that she is in need.

The provisions of the Statute have been from the inception, I think, unfair, inequitable and working hardship. They have made those provisions even more harsh by an amendment which was made in 1960. By the 1960 Statute they added the words "and indefeasible" meaning, presumably, that if there was a right of encroachment, of course, the gift could be defeated by the capital of the estate being applied under the power of encroachment.

I had correspondence with the Department some years ago, and the Minister wrote to me and said "Well, that has been modified". The modification was this: In 1962 --- 1963, they passed an amendment which provided

that the trustees could renounce the right of encroachment. They administer that in this way: If Mrs. Smith thinks she can get along on a certain amount of encroachment, say, a thousand dollars a year or two thousand dollars, or five thousand dollars, whatever it is, she can renounce any right to the capital over and above that.

Well, that puts the trustees in an impossible situation. Now, in the first place, perhaps I should say I am not arguing that in the case of the widow, for example, being the sole executrix and being given the right of interest with power to encroach that that should not be treated as an outright gift to her. Obviously she could say "Well, I will take the whole estate." I don't quarrel with that. To get over that position most people making a will put the widow in as an executor but also put strangers so it is not the discretion of the widow which has to be exercised, it is a number of executors.

Now, while the executors may have the legal power to say, "We will renounce the right to encroach on capital, or a certain part of that", they obviously cannot do it without discussing it with the widow and getting her consent. Even then they are departing from the wishes of the testator.

Now, in Ontario they deal with the matter on what is, I think, a fair and equitable basis. They say, "We will tax according to the event." They keep the estate open as long as the life interest lasts if there is encroachment, then they tax accordingly as if that had been left outright to the life tenant. To protect

themselves on that, they either do not release a certain portion of the assets or they ask for security to be furnished by way of bonds, perhaps estate bonds may be deposited with the Provincial Secretary. The interest goes to the estate and the treasury and the Government are protected and get whatever is the fair tax.

To show, Mr. Chairman, that I am not exaggerating in what I say, I could give you instances of six or seven estates. I won't name them, because some of them are sub-judice. Of course they will have the record in Ottawa. In one estate this method of applying the Act takes nearly $50,000.00 away from the charities in a case in which there was no encroachment at all. The life tenant died about a year after the testator and got no encroachment, asked for none, and yet the whole fund in which he had a life interest was treated as if it went to that life tenant.

A more extreme case, I don't even know the name of this one, but the Department will know, is one in which the life tenant of a fund died within a week of the testator. He probably didn't even know what benefit he was entitled to. In that case the estate was taxed as if that life tenant, who only survived the testator by a week, took the whole of that fund outright.

I could go on with these cases, Mr. Chairman, in which substantial sums are taken away from charitable organizations through something that I submit is completely artificial, unjust, and an inequitable method of taxation. I simply ask that it be put on a fair basis without the Crown running the slightest risk of losing the proper tax,

and that this iniquitous provision be altered. I say "iniquitous" in all good faith, because I cannot see any possible justification for it.

THE CHAIRMAN: Thank you, Mr. Cassels. I think we have your meaning and your feeling about this matter. You suggest an amendment to the Estate Tax Act which, as I understand you, is to bring it somewhat in line with Ontario. I am curious as to whether the law in Ontario provides a model for the amendment that you would have in mind, or whether it is a practice in Ontario which is not supported by any particular law.

MR. CASSELS: I think under the Ontario Act, Mr. Chairman, that this is the normal practice. If it was desired to amend the Estate Tax Act to provide the same system it could be very easily done by a small amendment to the Estate Tax Act.

THE CHAIRMAN: Would you proceed? What kind of amendment?

MR. CASSELS: Well, one was suggested by the Canadian Bar Association. I haven't studied it very carefully. This is the amendment to Section 7, which is the Section I am discussing. It is as follows:

> "Where any gift was made by the deceased during his lifetime or by his will to a donee described in Paragraph (d) of Subsection (1) but subject to a power in favour of any person to appropriate at any time or from time to time the whole or any part thereof for the use or benefit of any person, the gift so made shall not be considered to have been absolute and indefeasible,

except to the extent that such power is exercised at any time."

COMMISSIONER GRANT: Excuse me, Mr. Cassels, I have the amendment before me too and I believe you left out a word. There is a double negative there. "The gift so made shall not be considered not to have been absolute and indefeasible ---"

MR. CASSELS: That is correct, Mr. Chairman. Did I not read the double negative? With great respect for the draftsman of that, Mr. Chairman, there is one point that bothers me about it, and that is that word "any other person", because it could apply, the doctrine or principle that I am submitting could only apply in the case, as I said, of there being other trustees and not the widow alone. I just wondered if that word "other" would be inappropriate in the event of the widow and, we will say, two other people being the trustees. I guess actually they would be acting in a different capacity. The widow would really be in two capacities, one as a member of the Board of Trustees and in the other as a beneficiary, so it really would be "others" dealing with the trustees as a separate body.

COMMISSIONER GRANT: It would seem to be that "other" is used advisedly.

MR. CASSELS: I think so, Mr. Chairman. It bothered me a little bit in reading over that draft suggestion.

THE CHAIRMAN: Would you give us particulars of what you are reading from so the record may be complete.

MR. CASSELS: This is in the Canadian Bar Journal,

Volume 5, number 2, of April, 1962.

THE CHAIRMAN: Thank you, Mr. Cassels.

MR. CASSELS: May I add one thing, Mr. Chairman, which perhaps I should have done at the outset. I have not spoken to or canvassed a number of other organizations which I know would be sympathetic to the submissions made on behalf of the University of Toronto. One I have always been closely associated with is the Inter-Church Committee on Legal Affairs. I spoke to the Chairman of that body, and they are in full accord with the submissions that are contained in the brief. It is a little committee we formed a good many years ago with representatives of the Anglicans, Baptists, Hebrews, Presbyterians, Salvation Army, and the United Church. We have been able from time to time to help in matters of taxation. They are fully in accord and I am perfectly sure that other organizations will probably be making submissions to you later.

Thank you for your kind remarks about the University, Mr. Chairman. I will pass those on. I don't know if it would be fair to say I am entitled to credit on my argument for the rent!

THE CHAIRMAN: Have you anything further?

COMMISSIONER GRANT: Possibly the reason that Ontario assessed in the manner in which they do, which is favourable to the charity involved, is because of the very nature of the Act. It is a succession duty act, whereas under the Federal Statute it is an estate tax act, and as such the estate is charged with the payment of the duty. Would you agree, Mr. Cassels?

MR. CASSELS: Actually with great respect, no, because they have already shown that they want to benefit charitable institutions. If there were not the deduction for charitable institutions, then I would say "Yes". It is shown quite clearly they have them in mind and intend to benefit them. Does that answer your question?

COMMISSIONER GRANT: Yes. I think it is not too material the avenue in which it is approached, but it is the end result we are looking for.

MR. CASSELS: Yes.

COMMISSIONER GRANT: And if the amendment as proposed were to be made to the Estate Tax Act, then in your opinion, although you didn't give it a great deal of study, you would say it would go towards fulfilling your suggestion.

MR. CASSELS: Yes, Mr. Chairman. I don't know whether I should ask this indulgence. I would like to have the chance to study that matter further and perhaps at a later date submit a draft amendment.

THE CHAIRMAN: We would be very grateful if you would do exactly that.

MR. CASSELS: Could I speak to the Secretary and find out when I could submit the proposed draft?

THE CHAIRMAN: You can submit it any time you wish to do so in writing, rather than appearing. If you think it desirable to appear, you better then address yourself to our Secretary.

MR. CASSELS: It will take a little time. I think I will have to speak to a number of the Trust Companies and their solicitors to just insure that it

carries the blessing of all.

THE CHAIRMAN: Take all the time you wish.

MR. CASSELS: I would be very glad to do that if I may.

THE CHAIRMAN: It would be very helpful to us if you would.

COMMISSIONER GRANT: In drafting an amendment perhaps you will give consideration to the elimination of the double negative, which I have always regarded as an unfortunate thing where it does occur. I am wondering if the end result would not be the same if the amendment read "gift so made shall be considered to have been absolute and indefeasible."

MR. CASSELS: There should not be a double negative. That is a typographical error. "Gifts so made shall not be considered to have been absolute and indefeasible, except to the extent such power is exercised at any time." When you caught me on that, I must have read it as I understood it to be without noticing the second "not". It certainly should not be there.

THE CHAIRMAN: We will refer that to our Department that takes care of double negatives!

COMMISSIONER BEAUVAIS: I have just one question to ask: In many cases it would delay the final settlement of the estate for many, many years.

MR. CASSELS: Mr. Chairman, the Government does not suffer with that. I was speaking to one of the senior officials in the Ontario office this morning and it works admirably here.

THE CHAIRMAN: You don't see any difficulty?

MR. CASSELS: Not the slightest. Perhaps this is an unfair statement, but the only provocation for the present thing is what someone called "administrative ease". That was the unkind way in which it was defined to me.

THE CHAIRMAN: We thank you very much indeed, Mr. Cassels, for bringing this to our attention. We will certainly continue to give it our consideration and we would be very glad to hear again from you should you wish to put anything in as to a proposed amendment. Thank you, sir. We find it interesting and constructive, and indeed useful to us.

MR. CASSELS: Thank you very much.

THE CHAIRMAN: We will stand over for two minutes.

---Short Recess.

---EXHIBIT NO. 78: Submission of Mr. J. S. Robbins.

THE CHAIRMAN: Mr. Secretary, are we ready?

THE SECRETARY: All ready, Mr. Chairman. We now have a brief being presented to the Commission by Mr. John Stanley Robbins of Dundas, Ontario. Mr. Robbins is a sales tax consultant and he presents this brief on his own behalf.

I would like to enter it into the record as Exhibit No. 78.

THE CHAIRMAN: Good morning, Mr. Robbins. Thank

you for your submission and your attendance this morning. Most people appearing before us speak to their submissions. There is certainly no need to read it, as we have all read it already.

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I wonder whether we could properly take this section by section. I think we could quite nicely. Section 1 deals with certain subject which I would like to look at. Have you anything you would like to say to us before we start asking questions?

MR. ROBBINS: Mr. Chairman and Members of the Royal Commission, I have gone over this brief after I had it all fixed up for you, and one point here that I would like to bring out is this: The unlicensed branch that is used by a lot of manufacturers.

Now, this unlicensed branch does not benefit the consumer in any way. It only gives the manufacturer a chance to get a deduction on his invoice for sales tax purposes, but it does not benefit the consumer in any way. That is why I suggest in the brief that if there if the rate of tax were reduced to 6%, 3% sales tax and 3% Old Age, that it would do away with this unlicansed branch which is iniquitous.

Now, as a Government auditor, 34 years in the Government's service, these firms that operated on this unlicensed branch, they wanted all the benefits of it, but they did not want to conform to the requiremants of this unlicensed branch operation with the result that as an auditor I found on numerous occasions that they were not adhering to the restrictions of this basis at all, which in my opinion just made it null and void as far as any common sense application of the tax law was concerned.

Section 21 of the Regulations states what a wholesaler is and what a distributor is, and what a retailer

is, and so on and so forth, but in my experience the Department never would define the distinction between a distributor and a wholesaler, because the line of demarcation there is so small, so narrow, that it was impossible to define it, with the result that a lot of distributors were getting away with paying tax on the wholesale value instead of on the value on which they were supposed to under Regulation 21 of the Act, which I disagreed with as an auditor, do you see.

That is one of the main points that I want to bring out for your consideration. That is the fact that if this tax rate were reduced to 6% it would eliminate all this wholesale branch business altogether, and firms doing business in volume, they get volume discounts, they get cash discounts, they get freight deductions if the freight is recorded on the office copy of the invoice, and in that way the consumer, the man who is actually paying the tax, and that is the man we are concerned about in this country of ours, is the man who has got to pay the bill, and he would not be called upon to pay this iniquitous rate of 11% sales tax on the merchandise that he buys.

In my opinion, as I mention in my brief, that is just not fair, and that is the one point that I wish you would consider if you will.

THE CHAIRMAN: You do not need to stand unless you wish to, Mr. Robbins. Supposing I mark the unlicensed wholesale branch as item number 5 and we deal with these in order as they arise. The matter of 6% instead of 11% tax comes up under Section 2, I think.

COMMISSIONER WALLS: Page 4 is where that comes in.

THE CHAIRMAN: That is still Section 2.

COMMISSIONER WALLS: I think you have to take Sections 1 and 2 together really.

THE CHAIRMAN: Just reading the references, I thought I would suggest that we look at the unlicensed branch after we finish the other items that I referred to in here.

MR. ROBBINS: Very good, sir.

THE CHAIRMAN: I think we will deal with Sections 1 and 2 together. I do not think there is anything in Section 1 that is not referred to again in Section 2. I was a little surprised that you refer to this as a tax on industry, rather than a tax on consumers.

I suppose one could think of it as a tax on industry passed on to consumers, but I would be a little concerned as to who actually would bear the tax. I thought in most cases it passed through to the consumer.

MR. ROBBINS: All the tax now under the Excise Act is at the manufacturer's level. It is not on the consumer level; therefore the manufacturer under the Act is required to pay the tax to the Crown and his monthly tax returns. That is why I mentioned that. On the consumer level, like this Ontario retail sales tax, they are charging tax on a pyramided value from 200 to 300% on the manufacturer's level, which in my opinion is not fair to the taxpayer, but of course we are not dealing with Provincial matters; we are dealing with Federal matters.

THE CHAIRMAN: I think you missed my point. I was dealing with the manufacturer's tax, and I was merely asking you whether you did not feel that the manufacturer's tax was borne by the consumer, rather than by the manufacturer. Is it not passed through various stages until it arrives at the consumer, and the consumer pays more for his goods because of the tax than he would otherwise?

MR. ROBBINS: No, the manufacturer has the right to pay all taxes on his invoices on the basis of 11/111ths of the selling price after taking out volume discounts, cash discounts, freight and so forth, so that he is paying tax on the net value, you see. That price, for instance, is passed onto the wholesaler, and he puts his mark-up on and the wholesaler, when he sells it to the retailer, he puts his mark-up on, and when it gets to the consumer there is at least two mark-ups that are very distinct, on which it were applied on the consumer value, the tax would be on a pyramided value.

The basis of the Act all the years I was with the Ottawa Government was that it was not feasible to charge a tax on the consumer level. We had it in effect for several years, but the Department abandoned the idea because it was too costly. They could not see the reason for using it any longer, so they abandoned the whole thing and went back to the original sale price at the manufacturer's level.

THE CHAIRMAN: Thank you.

COMMISSIONER WALLS: I am afraid I am not clear yet. I do not think that you have given an answer to the

Chairman's question. Is it not a fact that a tax added at the manufacturer's level has pyramided and eventually the consumer pays that tax? We recognize, of course, under the terms of the Act the tax is paid either by the manufacturer, or in the case of imports by a licensed wholesaler in most cases, but when that is added to his price and the wholesaler then adds his percentage of profit to it, and the retailer adds his percentage of profit, is there not a chance that it is pyramided right through and the consumer eventually pays that tax?

MR. ROBBINS: The consumer pays the tax on the basis of the manufacturer's invoice to which is added, if he wishes to add it, but a lot of them don't add it. They include it in the price which means that any pyramiding is on the price charged by the manufacturer, which in a great many instances nowadays is on a tax-included value and not on a tax-extra value.

COMMISSIONER WALLS: If there was no sales tax would the manufacturer sell his product to the wholesaler for less money and the wholesaler would sell it to the retailer for less money if there was no tax?

MR. ROBBINS: Well, yes, the manufacturer --- if there was no tax he would not have a chance to charge, so therefore there would be no tax on the product.

COMMISSIONER WALLS: Then leading to my next question on the matter of exemptions, and I do not know that I altogether disagree with you on the extent to which exemptions have gone, but in the idea that this tax can be passed on to the consumer, should there not be some exemptions to avoid progressiveness? In other words,

you yourself mention on page 3, the disadvantage to the man with a family by having to pay sales tax on his children's clothing and shoes as against there being no sales tax on building materials.

MR. ROBBINS: Yes.

COMMISSIONER WALLS: Now, would you not say that if you were to remove the exemptions with the exception of those items that increase the cost to the low-salaried man such as food, clothing and perhaps drugs, that those might be logical exemptions instead of eliminating all exemptions?

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MR. ROBBINS:
Well, a manufacturer when he invoices merchandise that he makes, if he invoices that merchandise to some wholesaler who has a wholesaler's licence, no tax applies on that sale. The wholesaler - he buys that tax-free from the manufacturer under the wholesaler's licence so that when the wholesaler sells the merchandise out to the retailer, he accounts for the sales tax on the price charged to him by the manufacturer, or on the duty-paid value if the goods are imported into Canada, so that at no time is that price level disturbed from the standpoint of taxation.

COMMISSIONER WALLS: You still have not answered my question. Do you recommend elimination of all exemptions?

MR. ROBBINS: No, I am sorry; if I conveyed that impression I did not mean to convey that.

COMMISSIONER WALLS: Then your figures would not substantiate themselves wherein you state that if the tax was cut to 6% total instead of 11%, and I am including 3% Old Age Security Tax, that you would then have as much revenue as you have got today.

I worked it out, and the only way you would be able to do that would be by total elimination of today's exemptions, and I understood from your brief that is what you were recommending; total elimination of exemptions. The only way that you could cut your tax down to 6% from 11% and still have the same revenue would be by total elimination of exemptions.

MR. ROBBINS: What I meant by that was that if a manufacturer, when he orders merchandise, the component parts of the article he is going to manufacture, he would

be allowed, under the Act, to use his licence number to obtain all that merchandise tax-free so that he has got no money invested in sales tax up to the time of sale of the product that he is going to make.

Now, any of these firms that I mentioned in here as not having any licence at all, when they buy machinery and apparatus or ingredients or anything that is used directly or indirectly in the production of the goods that they manufacture and sell as unlicensed firms, our government has no access to check their records to ascertain whether or not those firms are entitled to obtain all the pipe valves and fittings that is used in the manufacturing operation tax-free, with the result that the Crown loses thousands of dollars of revenue for that very reason that the Government has no check. They have no authority to go in and check the records of the unlicensed firm.

I had a case in point just recently where I was in a big office and one of the purchasing agents mentioned to me, "You know, Mr. Robbins, in our certificate of exemption we state these valves - these regulators which we are ordering - will be used directly in production of goods for sale." They call them regulators; they don't call them valves any more, and Ottawa has authorized that, unfortunately, and that is what I took exception to, and I was working for the Government and I wrote to the Department and I asked them why they did it, and, of course, they didn't give me any answer because right there is a loophole, and this purchasing agent I was talking to just recently, he admitted to me

3 quite frankly that with that new regulation he is permitted, on ordering valves for his own maintenance - and these valves run at $800, $900, $1,000, $1,200, and $1,500 in lots of cases - he got those valves free of sales tax and the Government had no access to go in and check his records to see why he ordered them the way he did as a regulator when actually they are a valve.

COMMISSIONER WALLS: Thank you very much. Those are all the questions I have.

THE CHAIRMAN: I think we understand that point very clearly. Section 3, dealing with yarns. Again, it is quite comprehensive. I can understand the difficulty there, but at the present time I do not know what the solution is. Has anybody any questions on Section 3?

COMMISSIONER WALLS: The only thing I would like to remark: I think there is a justifiable case there because the same situation came up with respect to candy and it was ruled that if it was brought in bulk into Canada and packaged in this country, the packager became the manufacturer and paid sales tax, and I think that is something from Mr. Robbins' recommendations that we can very well look into.

THE CHAIRMAN: The unlicensed branch technique, of course, has been criticized by Professor Due and lots of other people. It has got some purpose, but perhaps as you say, it would not make any difference to the ultimate consumer and maybe it has outlived its original purpose; I do not know. However, it is certainly something that we assure you we will take a very careful look at. We have had quite a number of people suggesting

4 to us that the tax should be removed from the level of manufacturer's sales to the wholesaler to a different level, either the wholesale level or consumer level.

Have you anything to say on that score, Mr. Robbins? We know the difficulty which arose in the past. We are aware of the history that it was difficult to collect.

MR. ROBBINS: That is the point I wanted to make in my remarks here. I have, through experience, determined that the import of merchandise into Canada computed on the duty-paid value, the rate of tax applicable, worked out on the basis of the manufacturer, is about 6%.

Now then, my conclusion there is that if the goods manufactured in Canada - and after all, we have got to protect the Canadian manufacturer, like the textile industry that I mention here - you know what they have gone through. I have a client who is in the textile business, and I have been working for them for some time, and it is just very difficult to understand why they don't get more support from the Government than they do in these importations of this yarn, and these people are allowed to bring it in tax-paid on a duty-paid value, and yarn from Japan and these foreign countries, where the wages are low, this merchandise is dumped in here at a ridiculously low value. There is no dump duty put on it. To compete with that sort of thing the textile manufacturer is just up against it; he has got his back to the wall.

That is the point that I think should be looked

5 into very carefully by the Royal Commission and get an equitable basis worked out for the manufacturer against the importers that are coming in here.

For instance, I was in Ottawa six weeks ago for a firm, and they told me that my client would have to pay the sales tax on the packaging of the yarn that they sold from the manufacturing premises. Well, there is nothing in that Special War Revenue Act that says that tax applies on the packaging of yarn, and I told them so, and yet despite that they ruled this client of mine would have to pay sales tax on the selling price of the yarn which they packaged and sold to the Canadian trade and yet the importer, the unlicensed importer of this yarn, can bring it in and pay tax on this ridiculously low price into Canada with no dump duty on it at all. He then, of course, sells it at a much cheaper rate than they can afford to sell, and they get the business away from the manufacturer and the manufacturer suffers. I know several who have gone out of business as a result of it. That is the point that I think is most unfair and should be looked into.

THE CHAIRMAN: Thank you, Mr. Robbins. I can assure you we will keep this before us and we will consider it. We are grateful to you indeed for coming before us today, for your written submission and submitting yourself to the questions that we have put to you. We appreciate your long experience in the area of sales tax, and we shall weigh your thoughts and opinions most carefully, Mr. Robbins. Thank you very much indeed, sir.

MR. ROBBINS: Thank you, sir.

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THE CHAIRMAN: Is there anything more for us today, Mr. Secretary?

THE SECRETARY: Nothing, Mr. Chairman. Tomorrow morning at 9.30 the United Nations Association in Canada, followed by the Communist Party of Canada, and Mr. L.C. Foster.

THE CHAIRMAN: We will stand over until 9.30 tomorrow morning.

--- Adjournment

ROYAL COMMISSION

ON

TAXATION

HEARINGS

HELD AT
TORONTO
ONT.

VOLUME No.: 26

DATE: May 23, 1963

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ROYAL COMMISSION ON TAXATION

Hearing held in Howard Ferguson Auditorium, Sir Daniel Wilson Residence of University College, University of Toronto, Toronto, Ontario, on Thursday, the 23rd day of May, 1963.

COMMISSION:

MR. KENNETH LeM. CARTER -- Chairman

MR. J. HARVEY PERRY

MR. A. EMILE BEAUVAIS

MR. DONALD G. GRANT

MRS. S.M. MILNE

MR. CHARLES E.S. WALLS

LEGAL ADVISER:

MR. J. L. STEWART, Q.C.

RESEARCH DIRECTOR:

PROF. D.G. HARTLE

SECRETARY:

MR. G. L. BENNETT

ROYAL COMMISSION ON TAXATION

HEARINGS HELD AT THE CITY OF TORONTO, ONTARIO

May 23, 1963

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TORONTO, ONTARIO

Toronto, May 23, 1963

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Association in Canada.

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Toronto, Ontario,
Thursday,
May 23, 1963.

A/MC/ss

---On commencing at 9:30 a.m.

SUBMISSION OF

THE UNITED NATIONS ASSOCIATION IN CANADA

APPEARANCES:

Mrs. Eileen Swinton

THE CHAIRMAN: Mr. Secretary, I think we are all ready if our visitor is.

THE SECRETARY: Mr. Chairman and Commissioners, this morning we have a brief being entered by the United Nations Association in Canada. Mrs. Eileen Swinton is present to speak to the brief. Mrs. Swinton is a member of the National Executive and Vice-President of the Toronto Branch of the United Nations Associations in Canada.

I would like to enter this brief into the record as Exhibit No. 79.

---EXHIBIT NO. 79: Submission of the United Nations Association in Canada

THE CHAIRMAN: Thank you, Mr. Secretary. Good morning, Mrs. Swinton. Don't bother standing, most people remain seated.

We have read your submission with considerable interest. It is a matter of some considerable importance to many worthy organizations and we would be glad to hear anything further you would like to say about this matter,

either in summary of what you put before us, or to amplify it. There is no need to read it, as we have already read it.

Do you have anything you wish to say?

MRS. SWINTON: I don't think there is anything I can add. I think everything is pretty clear, at least to my mind, I hope it is to those of the Commissioners as well.

THE CHAIRMAN: I think it is quite clear. There are one or two questions that we would like to put to you. We would like to know to what extent you believe those organizations which do not qualify for charitable donations, such as UNICEF, to what extent they have suffered because of this? Do you have any idea?

MRS. SWINTON: It is pretty hard to estimate. I don't suppose the increase would be tremendous. For instance, with UNICEF the largest proportion of money raised is raised during the collection at Halloween and the sale of Christmas cards. The donations otherwise received by UNICEF might amount to $20,000.00 or $30,000.00 a year, for which income tax receipts could be issued.

It is hard to say how much more could be raised. It is always, of course, an added incentive for people to give.

THE CHAIRMAN: I was wondering if you had any idea in mind of the difference it would be.

MRS. SWINTON: I don't feel I could estimate it, Mr. Chairman.

COMMISSIONER MILNE: You mentioned about the possibility of assistance by popular demand. I was

wondering, in taking your appeal to the Government, have you had the support of any other groups with you?

MRS. SWINTON: Yes, there are other groups who are interested in this, as you have probably noticed in the list of organizations I have mentioned.

COMMISSIONER MILNE: I meant in supporting your group in asking for this.

MRS. SWINTON: It was a little late to get other groups to come in on the preparation of the brief, but I have spoken to a number of people and they were certainly in favour of the matter in principle. They feel the Act is not too clear on this point.

COMMISSIONER WALLS: Can you foresee a general clause in the Income Tax Act that would do the things you want it to do, or do you not rather see the Government would have to give an approved list of the charities that it would be allowable to?

MRS. SWINTON: I think possibly the Government might have to approve each individual charity, but I think the Act could be a little more specific than it is as to what might qualify. Certainly the United Nations charities or various projects that come up from time to time in aid of United Nations appeals might be specified within the Act.

COMMISSIONER WALLS: You can't just open the door.

MRS. SWINTON: No, I quite realize that. I think if the Canadian Government is strongly in support of the United Nations, as it always claims to be, and all parties claim to be, I feel this is one way they could

indicate support and permit individuals to indicate their support as well.

COMMISSIONER WALLS: Would you suggest any limitation as to the percentage of revenue raised that should be spent within Canada?

MRS. SWINTON: I feel at the present time, Mr. Chairman and Commissioners, that this is not relevant any longer. I think we recognize that charity is necessary abroad as well as at home, therefore, I don't think this should be specified.

COMMISSIONER WALLS: Do you think any of the charities that are today excluded have suffered in their collection in Canada because of lack of tax benefit?

MRS. SWINTON: To a certain extent. I was involved with the World Refugee Year Campaign a couple of years ago, and it did suffer in the early months considerably. We did finally get the exemption, of course. We picked up some of what we lost, but some I think was lost irretrievably.

THE CHAIRMAN: You got the deduction despite the limiting words "in Canada"?

MRS. SWINTON: Yes, it was a tremendous struggle.

THE CHAIRMAN: I was wondering how the Government could accomplish what you wish when the Act says: "in Canada"? It is organizations in Canada, not necessarily money spent in Canada.

MRS. SWINTON: Yes. The Act does not specify that it must be abroad. It took months of pressure for the World Refugee Year from a number of organizations and individuals.

THE CHAIRMAN: What you ask for would be accomplished by removing the words "in Canada" in 27 (1) (a).

MRS. SWINTON: Yes, I would think that. I don't presume to be an expert on the drafting of the Act.

THE CHAIRMAN: "Organizations in Canada", it seems to imply the money be spent in Canada.

MRS. SWINTON: Yes, and apparently that is the interpretation that the administrators of the Act take.

THE CHAIRMAN: Yes.

MRS. SWINTON: It could say to charitable organizations situated in Canada.

THE CHAIRMAN: I would think if it is the intention to deal with all charitable organizations at the discretion of the Minister, the words "in Canada" are redundant and should be taken out.

MRS. SWINTON: That again leaves it entirely to the discretion of the Minister, which in many cases is not too desirable

THE CHAIRMAN: Virtually it has to be there, does it not, or there would be charities that should not qualify because they may bear the name of charity and may not in fact be genuine.

MRS. SWINTON: Yes.

COMMISSIONER WALLS: Unless you listed the charities, would it not lend itself to fictitious charities and sending tax-free money out of the country.

MRS. SWINTON: Well, there surely could be adequate safeguards for that type of thing. You can look into the sponsorship of any charity before it is accepted.

COMMISSIONER PERRY: This is probably a silly question, and I only ask it because the brief does not specifically answer it: Can we assume exemption has been requested for all these various organizations and refused?

MRS. SWINTON: Yes.

COMMISSIONER PERRY: Is there any indication in the refusal of the grounds for the refusal?

MRS. SWINTON: Just that the money is spent abroad.

COMMISSIONER PERRY: There is a possibility, you know, that the Treasury attitude creeps in here. There may be some feeling that since the Government is already supporting the United Nations directly that it need not also do so through an income tax deduction.

MRS. SWINTON: No doubt this is their attitude, but the more money raised voluntarily for the United Nations means possibly less pressure on Government to make Government contributions.

COMMISSIONER PERRY: Yes, there is the idealogical inconsistency here, although the Minister of Finance might feel it is a strong argument.

MRS. SWINTON: It is mainly the fact it is inequitable, because so many charities do the same type of thing and they do have the exemption. If the United Nations charities are refused, so should others be refused if that is their ground on which they are refused.

COMMISSIONER PERRY: It is quite interesting that the United Nations organizations as a group have been refused. There may be a little bit of this attitude behind the refusal, because any Minister of Finance would say "I am not going to pay for this both ways." I am not defending that attitude, but I think some of it might be present.

MRS. SWINTON: It is really unfair that the churches and various groups who raise money for the same projects can issue receipts in their names. For instance,

there are all sorts of organizations raising money for Freedom From Hunger and all except the Freedom From Hunger Committee itself can issue receipts.

COMMISSIONER PERRY: I suppose the money that goes abroad to the foreign missions from Canadian churches would far exceed anything that any other organization would be contemplating.

MRS. SWINTON: Yes.

THE CHAIRMAN: I think we fully understand what the problem is, Mrs. Swinton. We will certainly consider it further. Thank you very much for putting it before us, and for appearing here this morning. You have done the job so tidily that we have got through in a new record time.

MRS. SWINTON: Thank you very much.

B/ET/dpw

THE CHAIRMAN: Are we ready, Mr. Secretary?

THE SECRETARY: Yes. Mr. Chairman, Commissioners, you have now the brief before you from the Communist Party of Canada. Mr. Bruce Magnuson, leader of the Ontario Communist Party is here together with Mr. Alfred Dewhurst, Educational Director of the Party. Mr. Magnuson will speak to the brief which I now enter into the record as Exhibit No. 80.

--- EXHIBIT NO. 80: Submission of the Communist Party of Canada.

SUBMISSION OF THE COMMUNIST PARTY OF CANADA

Appearances: Mr. Bruce Magnuson
Mr. Alfred Dewhurst

THE CHAIRMAN: Thank you, Mr. Secretary. Good morning, gentlemen. We have read your submission with considerable interest. It covers quite a bit of territory, and obviously some of it is of more interest to us than others. As you will have observed by our terms of reference, we are appointed by the Federal Government to look at Federal Government taxes, and we are reluctant to go very far into the matter of Dominion-Provincial relations in taxation, and likewise into the matter of municipal taxation. However, there is a good deal of your brief which is, of course, most pertinent to our considerations, and I would like to address a few questions to you along the lines of that particular part.

Before getting into that, would you like to tell us a little bit about your organization, Mr. Magnuson? You are representing, I think, the Executive Committee of

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the Communist Party?

MR. MAGNUSON: That is correct, sir, yes.

THE CHAIRMAN: What is the Executive Committee? How does it come into being?

MR. MAGNUSON: Well, the Executive Committee of our Party is elected from a National Committee, which, in turn, is elected by a National Convention of the Party.

THE CHAIRMAN: The National Executive Committee appoints the Ontario Committee?

MR. MAGNUSON: No, the Ontario organizations of the Party have their own set-up; their own conventions. They elect their own committee, but I am a member of both. I am a member of the National Executive and also of the Provincial Executive.

THE CHAIRMAN: You have a Taxation Committee?

MR. MAGNUSON: We do not have any separate Taxation Committee as such.

THE CHAIRMAN: This brief is drawn then by members of your Executive Committee, I take it?

MR. MAGNUSON: That is correct.

THE CHAIRMAN: One thing you do not cover in your submission and which I was curious about is that my impression of the taxation in those countries where the Communist Party provides the Government that taxation is generally very low. We have got very little information about that. We know a good deal about Western European countries, but we do not know very much about the Eastern European countries. Can you tell us anything about that? Do you know what their tax systems look like?

MR. MAGNUSON: Well, no, I am afraid I would not

3 care to go into that very much because I am afraid I would not know enough about that to do so.

THE CHAIRMAN: I was curious and I thought I would ask you.

MR. MAGNUSON: I would be very happy, sir, to find out something for you if it would be of any assistance.

THE CHAIRMAN: If you have any literature on the subject I personally would like to get it and I am sure the other Commissioners would also. It has occurred to me that a principle of Communism, as I understand it, is that the Government owns the facilities of production and distribution. That being so, why taxation? It would seem to me that sufficient revenues can be secured for the purposes of government by the mark-up on goods in a more satisfactory manner than taxation, and therefore I did not see why taxation, and I was curious as to why you would come forward with a submission on taxation.

MR. MAGNUSON: Well, of course, if I may say this in addition to a few remarks I would like to make before we get into the questions: actually, on a long-term prospectus the idea is to do away with taxation as such. We do not favour taxation in the sense of continuing debts. We are living here in Canada, which is an entirely different situation.

COMMISSIONER WALLS: Would you please speak a little louder?

MR. MAGNUSON: I wonder if I may make a few remarks.

THE CHAIRMAN: If you would, yes, in your own way rather than in reply to my questions.

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MR. MAGNUSON: We take the point of departure here in Canada from the fact that it is virtually impossible today to speak of a proper and democratic tax system in this country. As long as we have an annual drain of somewhere around one billion dollars that flows out of the country annually in payment of interest and dividends and such commitments to foreign investors in this country; secondly, when we have some one-and-a-half to two billion dollars spent for what is largely wasteful expenditures, far beyond what is required for the country's actual defence purposes.

We have, over a long period of years, as a Party in this country, taken a position on this question of taxation and how it affects the economic and social life in relation to the development of the country and the productive capacity.

Now, if I may draw attention of the Commission, for example, to a brief we submitted here in 1937 to the Royal Commission on Dominion-Provincial Relations, which we received commendation for at that time. It is a rather large and documented brief that goes very exhaustively into the constitutional history of Canada and the difficulties that have arisen as a result of the growing economic developments here in terms of the governmental set-up that we have, Dominion, provincial and municipal.

We also submitted a letter or a document to the Dominion-Provincial Conference, 1955, among other things, and an extensive documented brief to the Gordon Commission on Canada's economic prospects, and a letter to the Prime Minister of Canada in 1960 at the time of the Dominion-

Provincial Conference. There are numerous other documents, too numerous to mention here, that we have submitted over the years dealing with this question.

Now, wages, as we see it as a percentage of national income, at times, particularly of economic expansion, has a tendency to decline relatively, particularly in periods of economic growth, and that the taxation is loaded onto the shoulders of those who are least able to pay.

As a matter of fact, in this country today we have a situation where much of the bigger corporate businesses have various means of evading taxation, and are given all sorts of leeways for the purpose of doing that.

I would like to draw your attention, for example, to the situation that is a point of reference here, to illustrate what I am talking about in connection with the annual statement of International Nickel Company of Canada. The International Nickel Company of Canada's annual statement here shows us that in 1961 their net earnings were $88,777,000, on which their income taxes paid were $60,876,000.

In 1962, a year later, last year, their net earnings were ninety-four-and-a-quarter million dollars, or just about that, and their taxes were down $37,429,000 as a result, of course, of the exemptions they gained as a result of the Thompson, Manitoba development.

Now, this company has a fifty-four million dollar tax reserve. As a matter of fact, this year they could go along without having to deduct anything from their earnings to pay their taxes, and while they have

6 something in reserve, they have taken out something of a billion-and-a-half worth out of the mining operations in Sudbury alone, and in the event that one may speak about this being an incentive to increase economic activity, I may point out that the company itself states here, on page 7 of their annual report, 1962, that having established large stand-by stocks of refined nickel, the company curtailed production at its mines and plants in Canada in the latter part of the year.

Now, of course, only about two-thirds of the money that I have mentioned here as being paid by income tax, paid as income tax by the International Nickel Company of Canada, is actually paid to Canada. Something like $27,000,000, I believe, or thereabouts. The balance of the taxes is paid to the United Kingdom and the United States. So that out of these large operations the Government gets comparatively very little of taxes, relatively speaking.

2 Now, if you take a worker's income, on the contrary a worker's income is very heavily taxed. As a matter of fact, it will take a worker a long time to earn his taxes and amounts to anywhere from 25 to 30 per cent of his income, the average worker, and that is what happens in the case where the wife is working. The worker has no means of escaping taxation because it is deducted at the source. As a matter of fact, in the case, for instance, of seasonal workers, the deduction that is based on the income tax regulations at the source is much higher than is required when his earnings are distributed throughout the year, and as such, constitutes the interest-

8 people in mental institutions and TB cases out of ordinary revenue, but this is not the case now. When the Government, now, in Ontario, speaks of a deficit in its operation of the Hospital Services Commission, as in 1960, for instance, $10,000,000, and in 1961-62, a little bit of an increase, and so on, this means lumping together all of those costs. This means, for example, that every taxpayer, even those who do not make enough now to pay taxes, now have to pay the same amount whether their income is $2,000 or $2,000,000 a year; not only towards maintenance of the health insurance scheme as such, for the protection of the person for which it was designed, but also for the mental institutions and for TB care which was formerly taken out of ordinary revenue.

Now, if this has to be resorted to in Ontario, just as an example, what about the other provinces which have much less means than the Province of Ontario has to undertake such expenditures?

C/MC/ss

I might also mention here the fact that more and more of the national tax revenue is taken over and appropriated by Federal Government and this is a direct consequence of the aims of our national policy today in Canada. The share of the tax revenue, relatively speaking, that comes to the local and Provincial Governments has declined while they call upon such Governments for social services which have greatly expanded during recent years.

Now, this is particularly true during the past fifteen years since 1947, when the policy of this country brought about a very rapid increase in the foreign investment, mainly investments from the United States in Canada. These investors are in a rather favourable position with regard to taxation as compared to those who are investing in Canada as Canadians. Of course, the fact of the matter is that as long as this policy continues the situation will get worse, and it will get more and more out of line with respect to responsibility for social services as the industrial operations expand and less and less revenue will be available.

Besides that, we must take into consideration the fact that it is impossible today for a municipality to take the responsibility for a national industry establishing a branch plant in its community which may go out of business very quickly. This is a national problem, but which may result in certain expenses which will be put on the back of the municipal taxpayer. Now, we have cases in Ontario, Windsor for instance, where industrial

activity has declined. We have the case of the uranium industry at Elliott Lake. We give that example as another case in point.

There is one other point I wanted to make, and that is with regard to ability to pay. I mean any taxation system which robs a person of the essential requirements of living. I refer to a workerwho has a limited income, and we know the distribution of national income in this country is extremely uneven. I could speak for hours on that if I could quote all the briefs and submissions to document what I am talking about. There are hundreds of thousands of working people in this country that don't make enough money to make ends meet, but are today called upon to pay taxes. This is a very unjust situation, to say the least.

On top of that now we have the sales tax coming into the picture, Federal sales tax and Provincial sales tax, all sorts of other taxes. It is this that is responsible for the fact that between April the 30th, 1961 and April the 30th, 1962, which are the latest figures available to me, the total personal debt of Canadians increased by 21.2% in one year. On this basis workers are living, working people are living that is true, but living on borrowed money and perhaps sometimes on borrowed time, and that is not a good healthy situation for the expansion of productive activity in the country. On the contrary, the way to guarantee debt is expansion of the domestic market and ability to buy back goods and pay for services.

This was evidenced very much by the fact that

in the war years, when we had the highest taxation also on corporate income as well as others, in this country the economic expansion was more rapid than at any other time. The increase in the national income from 1938 to 1945 was something like 144%.

Well, I think perhaps that will suffice to emphasize some of the main points that I wanted to draw to your attention with respect to our brief. Our brief is directed towards pointing out the necessity for a change in this country with respect to the taxation system, which comes up against social and economic conditions which compel many and varied reforms and changes also in the structure and functions of Governments. It is, I think, incumbent upon this Commission to recommend to the Government, and we wish that this would be given serious consideration, steps which would bring about that kind of reform of our tax system immediately, that is which will stop most of the loopholes for evasion of taxation by those who are best able to pay, and relieve taxation of those who are least able to pay. We recommend bringing about a kind of taxation system which will put taxation on the principle of ability to pay and bring about a situation also which would eventually help to bring into being a more just responsibility for social services. This, of course, requires constitutional changes and those constitutional changes might take a much longer time. It is a more complicated process and our brief points that out, I think.

We have not dealt in too much detail in this brief, as we did, for instance, in previous briefs because

what we are in most need of here is to deal with the principal questions of policy that are involved here, and without which it is impossible to get at any of the detailed matters, the technical questions that will have tobe answered.

THE CHAIRMAN: Thank you, Mr. Magnuson. Any questions?

COMMISSIONER WALLS: My first question deals perhaps with a section of your brief that is outside of our terms of reference. I was interested in your recommendation that the cost of education should be collected by the Federal Government and administered by the Provinces. Do you mean the entire cost of education, or do you mean the portion that is today collected by property taxes? In other words, in practically every Province of Canada today 50% of the cost of elementary and secondary education comes out of consolidated revenue and 50% comes out of property taxation. Now, would you have the Federal Government just collect the amount that is today collected by property taxation?

MR. MAGNUSON: Well, our proposals over a number of years have been concerned with the cost of elementary education, that is that the Federal Government should assume responsibility for the cost of elementary education, which is that which falls directly on the property owners.

COMMISSIONER WALLS: Elementary and secondary?

MR. MAGNUSON: That is true.

COMMISSIONER WALLS: But then the Provinces today are themselves paying out of the consolidated revenue

half of that cost, so I presume what you would have the Federal Government collect would be the equivalent of 50% of the cost?

MR. MAGNUSON: No.

COMMISSIONER WALLS: You would have them collect it all?

MR. MAGNUSON: That is right. We have made the proposal that the aim should be for the Federal Government to assume full responsibility for educational costs, both primary and secondary education. That is a step towards that. The very first step should be that the Federal Government should pay to the Provinces as a statutory right a sum equal to the amount required to meet elementary school costs, which in turn would be distributed by the Provinces to the municipalities on the basis of the number of pupils in the elementary schools. That would relieve, in other words, both the Provinces and the municipalities of the cost of education. We feel this way about it, because the Federal Government would be in the best position to see to it that there would be equal opportunities for all children across the country, as we feel there should be.

COMMISSIONER WALLS: My other questions may seem to jump back and forward across your brief. My second question deals with number 22 in your summary where you recommend five percent ceiling be placed on advertising. In other words, 5% of the operating costs of any company shall be the ceiling amount they shall spend on advertising. Are you not going to play into the hands of the well-established large companies by doing

that and make it difficult for new businesses to come on the market. If you are going to limit them to only 5% of operating costs, you are going to preserve the position of the man or firm that is already well established and make it practically impossible for a new product, a new competitor's product to come on the market against it; are you not?

MR. MAGNUSON: Well, I don't think the intention here is to propose something that will be necessarily applicable in all cases. What we are talking about here is a maximum ceiling, so to speak, on deductions which may be made for taxation purposes.

COMMISSIONER WALLS: Yes, but you do see where it is going to prejudice new businesses coming on the market if they are limited to 5%.

MR. MAGNUSON: Well, I do not see where that would make that much difference that it would hamper them in any way. I think there should be ample allowance.

COMMISSIONER WALLS: If I had a business with operating costs of a million dollars I would be allowed to spend 5% of that. Now, if my competitor came into the same line of business and his first year his operating costs were $100,000.00, he would only be able to spend 5% of that $100,000.00, which might make it impossible for him to get his share of the market. In other words, you would be preserving the position of the already well-established companies.

MR. MAGNUSON: Of course, I think here we have to take into account it would also work the other way around. We have too much excessive advertising today, and

the very idea that sales are made by advertising alone I think is fallacious. The question is the fact of people buying things perhaps they don't need through the medium of advertising. People buy because they can afford to buy, and they buy because they need to buy. In many cases today when there seems to be no limit I would think that a small business or a new business would be largely hampered by the excessive amount of advertising that larger businesses are able to carry through and they cannot compete. Some limit should be placed on that. There should be some assistance in that case. It could work also the other way around.

COMMISSIONER WALLS: Then some of your criticism in respect to collection of salary and wage earners' income tax at source is quite justified, but do you not believe that most wage and salary earners prefer this system of paying income tax by deduction as earned, rather than having to pay a lump sum at the end of the year?

MR. MAGNUSON: Well, I think to the extent that they have to pay taxes it doesn't make too much difference to a worker. It perhaps will be easier this way if it is deducted piecemeal. The fact of the matter is that many workers today are paying taxes who should not actually pay any taxes at all, and that is where the difficulty comes in. Now, this applies in general, for example, as a result of the low exemptions which we are asking today should be raised, which would except hundreds of thousands of workers from paying income tax in the first place. I am referring to people in the timber industry, for example, who are seasonal workers and other people who are

deducted because, say, for a few months of the year their average income is fairly high and they come under certain income tax brackets and they are deducted. After that they don't work for a number of months and as a result of that, when their income is averaged out for a year, they are entitled to a refund. This tax has gone to the Government and is being held there, and while they do get a refund, they have to wait a long time before they get it.

COMMISSIONER WALLS: Would you not consider that even if the changes that you desire are put into effect, of larger deductions for those who will continue to pay income tax that the wage earners will prefer the system of paying as they earn it, rather than as a lump sum?

MR. MAGNUSON: I know, of course, that most workers I am sure do not prefer to pay any taxes.

COMMISSIONER WALLS: Of course that is trueof
3 all of us, I suppose.

MR. MAGNUSON: But as I said to the extent that they have to pay taxes this is probably as good a way for them as any to pay.

COMMISSIONER WALLS: I notice you suggest that we cancel the Federal sales tax on consumer goods. Now, how would you draw a line of demarcation within the taxable goods that are under Federal sales tax today as between consumer goods and capital goods? Is it your intention really that the whole tax be taken off, or just be taken off certain types of goods?

MR. MAGNUSON: We think that taxes, such things as sales tax should be taken off consumer goods entirely.

COMMISSIONER WALLS: For instance, is an automobile consumer goods? Is jewellery consumer goods? Are radios consumer goods? I am not trying to get you into difficulty, but I am trying to get you to help us to draw a line of demarcation on what are consumer goods.

MR. MAGNUSON: I think the automobile today is no longer a luxury, but a necessity for a person to have. It is part of his life. It is part of the worker's life commuting to and from work, and it is certainly a very important factor when it comes to excise tax and sales tax being added onto such items which enter into the ordinary living.

COMMISSIONER WALLS: You then go on and favour the continuation of excise tax. In one paragraph you say you wish to take off the sales tax on consumer goods and in the next paragraph you deal with the continuation of the excise tax, but you do not exclude the consumer goods that fall within the excise tax. By that I am referring to things like shaving soap and your wife's lipstick and radios. All of these things are today subject to excise tax. Now, you wish the excise tax to continue?

MR. MAGNUSON: Which part of the brief are you referring to, by the way?

THE CHAIRMAN: 44 and 45, page 10.

D/ET/dpw

COMMISSIONER WALLS: You say excise taxes should be levied only on the value-added basis. I am going to come to dealing with the basis of tax in a minute. In other words, you wish excise taxes to be continued but you made no qualification on the excise taxes as you did on the sales taxes. On the sales tax, you said it should be removed from consumer goods, but there are some consumer goods that are excise taxed.

MR. MAGNUSON: That is true, but there are very complicated problems involved here in terms of imports and exports, particularly in Canada, where we have branch plants operating of foreign corporations, that are importing component parts on all of this kind of business. One would have to be very technical in order to go into that.

We are not in favour of excise taxes,as such, on consumer goods either. Anything that will add in cost in this sense to consumer goods should be limited, or over a period of time abolished and replaced by more equitable taxes such as capital gains tax which we are talking about in our brief.

COMMISSIONER WALLS: Of course, I was only going by your statement in this paragraph where you said excise taxes should be levied only on the value-added at each stage of production and distribution from the manufacturer's price to the final sale to the consumer.

MR. MAGNUSON: Yes.

COMMISSIONER WALLS: And the point I want to find out from you whether you w nted consumer goods excluded from that the same as you have it from sales tax.

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MR. MAGNUSON: Well, of course, it does not say so here.

COMMISSIONER WALLS: No.

MR. MAGNUSON: That is so, it does not say so, but what we are dealing with mainly in this paragraph is the question, of course, of adding taxes on top of taxes.

COMMISSIONER WALLS: I appreciate that. Well then, through sales tax today we collect some three hundred million of the Old Age Security tax. Now, if we take a very large percentage of the sales tax off, where would we now collect these hundred millions of dollars for Old Age Security? Would you add that to income tax?

MR. MAGNUSON: I would think so. If they would carry out the provisions that are in principle outlined in this brief, there could be a considerable increase in the revenue that is collected by the Government to cover social expenditures without having to pin it on those that are least able to pay.

COMMISSIONER WALLS: How do you see the value-added tax being used for excise?

MR. MAGNUSON: I don't quite get you.

COMMISSIONER WALLS: In your brief, you wish to employ the value-added method of collecting excise tax.

MR. MAGNUSON: Oh, yes.

COMMISSIONER WALLS: Now, how do you see that being employed?

MR. MAGNUSON: Well, of course, this has to do with the question of income, what constitutes income in productive activity; capital appreciation, if that is taxed, in addition to the value that is added in the course

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of production in terms of income tax, that is going to produce a lot of revenue that is not now collected.

COMMISSIONER WALLS: I just have one other question, and perhaps I am taking too many questions from my colleagues.

THE CHAIRMAN: Oh, no.

COMMISSIONER WALLS: See if I have this right: I am rather concerned about where we are going to get all the money to do all the things that you have recommended here. Firstly, you are suggesting that the Federal Government collect sufficient to pay for the cost of elementary and secondary education; secondly, that they collect sufficient to pay 80% of a national health plan; third, that we remove a very large percentage of the sales tax; fourth, that we increase the basic exemptions on income tax, and fifth, that we deduct the taxes on assessed values of homes up to $5,000.

Now, against that, the only place that I see you are recommending an increase of taxes to cover these things is capital gains tax, a heavier tax on higher income tax brackets, and increased tax on dividends going out of the country.

Have you made any estimate of what the total cost is going to be of those increased services that you want the Government to carry out, and as to whether they could be applied to these three increases in taxes?

MR. MAGNUSON: We do believe that if those steps are taken there would be sufficient revenue to meet the requirements.

COMMISSIONER WALLS: I would conservatively

4 estimate it is going to take somewhere between two and three billion dollars, and I just cannot see how you can make these additions to the three existing taxes that you suggested and be able to get that amount of money.

MR. MAGNUSON: There is a lot of income to be derived in terms of taxation on capital gains, net worth, capital appreciation. As far as dividends on investments, foreign investments in the country, there is another source which will bring about a considerable amount.

I want also to mention, for instance, that you already had a brief from a gentleman here the other day, I believe, who said that sales tax now only covers 50%
2 of the firms; where manufacturers of agricultural equipment, chemicals, building materials, fancy biscuits and so on were exempted.

COMMISSIONER WALLS: What he meant was partly what you are already asking for; a very large percentage of consumer goods have already been exempted from sales tax. 50% of the total items are today exempt, and a very large amount of these are upon consumer goods.

MR. MAGNUSON: Yes, but actually I do not have his brief. I read a report of it to mean the opposite, the fact that sales tax in its application is not applied in many cases where it could be applied without entering into the consumer goods field. If that was not the case, then, of course, that is another matter.

COMMISSIONER WALLS: That is all, thank you.

COMMISSIONER PERRY: I have one or two points. Although as the Chairman said we are not going very deeply into the Federal-Provincial area. You do make a point

that the constitutional distribution of taxing powers should be revised.

I was just wondering if you had anything in mind in respect of the federal taxing powers which are now, as you know, unlimited.

MR. MAGNUSON: Well, when you speak of unlimited federal powers of taxation, I do not think that it is entirely correct to speak of unlimited federal powers of taxation in the present circumstances in the sense that the provinces enter into the picture, and under our constitutional set-up, it depends on what is taxed and how it is taxed.

THE CHAIRMAN: I cannot hear you.

MR. MAGNUSON: It depends on what kind of taxation. In the income tax field, for example, as opposed to real estate, as opposed to property taxation, and so on; corporation income tax.

COMMISSIONER PERRY: I think you are speaking more of the practical application of the taxing powers, and I am quite sure that the constitutional position is that the Federal Government has full rights to impose any kind of tax.

MR. MAGNUSON: If that is so, under the present circumstances, then it could be done; to make it possible for the Federal Government to assume those services which we propose in the brief here should be the concern of the Federal Government.

COMMISSIONER PERRY: So that when you speak of constitutional change, you do not have any change in mind for the federal powers of taxation? I am being a bit

6 sticky about this because I do not think, in fact, you have used "constitutional" in the same sense that I would. I have in mind the provisions of the British North America Act which is our constitution in this sense, which sets out the respective taxing powers of the national government and the provincial governments.

When you speak of changing the constitutional arrangements, I interpret that as changing those sections of the British North America Act, not changing the kind of tax which each Government is levying at any particular point of time.

MR. MAGNUSON: Well, we believe, of course, that we need a new constitution.

COMMISSIONER PERRY: People have been saying this for at least 50 years now, and nothing very tragic seems to have happened in the absence of a new constitution, particularly in this area, in taxing.

However, on an entirely different subject, do you have any views as to the incidence of the corporation profits tax? Do you have any views as to where this tax finally lands, whether it is on the shareholders or the consumers; whether it is passed on to the consumers? We have had many conflicting views presented to us, and, of course, one's attitude towards corporation profits tax would be quite different, depending upon one's views as to its incidence.

MR. MAGNUSON: Well, of course, that is one of the reasons why we feel that capital gains tax is so important. We also feel that the corporations' income taxes should be much stiffer and more strictly applied.

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Now, of course, it is true that in many cases, and no doubt in most cases, there is a tendency for this to be passed on to the consumer in one way or another. In that sense the capital gains tax will help to balance the situation much better, and a gradual shift in that direction will be an improvement in our tax structure from the point of view of shifting the taxes to those who are better able to pay. Otherwise, it is being passed on through various ways and means, including all the various corporations, at various stages passed on to those who are least able to pay.

COMMISSIONER PERRY: So that you think that some part of the corporation profits tax is passed on?

MR. MAGNUSON: Yes, we certainly believe that.

COMMISSIONER PERRY: Well, of course, one would not condone any form of evasion or avoidance of tax, but on the other hand, if it does happen that corporations minimize their tax, then in your view it should follow that they are minimizing the taxes that are being passed on?

Now, on a completely different area again, do you feel that the social benefit program and the tax burden should be kept in entirely separate compartments, and no account taken of one in viewing the incidence of the other?

Just take the hypothetical possibility, for example, that the whole of the tax revenue were converted into a massive social security program for people with incomes under $5,000. The Government spends all its money for this purpose. Would you then go on looking

8 only to the burden of the taxes that were imposed as the measure of a democratic tax system where the benefits received might be ten or fifteen times the amount of the tax being levied?

MR. MAGNUSON: Well, I do not think, hypothetically, or in any other way, that such a situation is very realistic. Therefore, in the first place, all the revenue of the Government cannot be applied in that sense.

COMMISSIONER PERRY: Well, let us say 15% to 20% applied that way. That is getting closer to the present position.

MR. MAGNUSON: One thing we do know is that in the present situation of distribution of national income,
3 the way it is, private ownership, all of the means of production in the hands of fewer people and higher centralization of control of finance and industry in the country, with the requirement of social services, the costs of such services are continuously increasing, and at the same time people who are in control of governments and who determine the policy of governments and so on are in an increasingly stronger position to determine ways and means of evading it.

COMMISSIONER PERRY: There is a real problem here as to how far ultimately you must take into account the benefits, the direct cash benefits of a program of government expenditure.

E/MC/ss

Any level of income where the taxes are being paid may be just a small part of that direct benefit. With regard to money leaving the country you say you feel this should bear the same burden as if it had been received by residents of the country. I suppose you have in mind there that non-residents should be subject to some sort of a graduated withholding tax or a tax something like our personal income tax.

MR. MAGNUSON: Something like that, yes.

COMMISSIONER PERRY: This is not an unprecedented suggestion. There are some countries which do have this practice. They require the non-resident to file a return and pay tax as though he were a resident in the country of origin. Have you thought much about the practical implications of your tax on capital gains which, as stated in your brief, would apply both to realized and unrealized capital accretion? To my knowledge, no country has attempted to get at the unrealized accretions and there are enormous problems not only of evaluation, but reporting involved. I think you would have to have an open account for two or three million taxpayers with an annual appraisal of their total net worth. Is this the sort of thing you have in mind?

MR. MAGNUSON: Well, of course, as far as the actuarial problem, the technical aspect, is concerned, I am in a very poor position to speak on that, because I am neither an accountant, nor a person who aspires or can claim to be an economist in the sense I would be able to deal with the detailed application of it. We are concerned mainly here with the principle that is involved,

and what would be just an equitable in terms of treating capital appreciation.

COMMISSIONER PERRY: Without reflecting on the validity of your proposal at all, I think you would have to agree that some things which are theoretically ideal just cannot be worked out in practice, and this might be one of them, particularly where you are referring to unrealized gains.

MR. DEWHURST: It would be practical on the realized.

COMMISSIONER PERRY: There are taxes in existence which do operate on realized gains, yes.

COMMISSIONER BEAUVAIS: You state in your summary at 17 B that increase in net worth is exempt from taxation. Well, if the increase represents the savings in wages or salary of a man on which income tax has been paid, it seems to me that this increase in net worth has been subject to taxation.

MR. MAGNUSON: There is no doubt about the fact that there may be here a bit of overlapping. It depends on how it would be applied actuarially speaking, but this is not the kind of net worth we are so much concerned with. It is the big aggregations of earnings of capital appreciation that we are concerned with, increasing net worth that is not subject to taxation and speculative capital and everything else that comes into the picture.

COMMISSIONER BEAUVAIS: Nevertheless you do admit that if it is due to dividends or wages or salary on which tax has been paid, this increase in net worth has

been subject to tax.

MR. MAGNUSON: Yes, that might be. As I said, there might be an area of overlapping there, but I don't think that would be serious.

COMMISSIONER BEAUVAIS: Section 38, page 9, you say the great accumulations of wealth which exist today are held by corporations and therefore not accessible to succession duties. The shares of those corporations are held by individuals and when a shareholder dies, then his share is valued according to that wealth. In effect, that wealth is accessible to succession duties; is it not?

MR. MAGNUSON: I am afraid I didn't quite get your point.

COMMISSIONER BEAUVAIS: A shareholder of a corporation has part of the wealth of a corporation and when he dies his share of that corporation is evaluated and then his estate pays succession duties on that value. Therefore, this wealth is accessible to Estate Tax.

MR. MAGNUSON: In that limited sense, yes, I would think so.

COMMISSIONER BEAUVAIS: In section 39, Commissioner Perry talked about your suggestion of taxing both realized and unrealized capital gains, but would you consider also allowing for a decrease in value in the capital assets? For instance, if a property is valued at $100,000.00, and is worth $120,000.00 at the end of the year, according to your suggestion he would pay taxes on the $20,000.00, whether it is realized or not. Now, if it is proven this property is worth $80,000.00, would you

then allow $20,000.00 against his other income?

MR. MAGNUSON: Well, of course that is a question that is very hard for me to answer how that would be treated in that case. I am afraid I can't answer that.

COMMISSIONER GRANT: You said that 25 -- 30% of workers' income was paid out in the form of taxes. Were you referring there to all levels of Government that impose taxes, or were you referring only to the income tax?

MR. MAGNUSON: I was referring to all levels of various indirect taxes that the workers pay.

COMMISSIONER GRANT: Including municipal taxes and real estate?

MR. MAGNUSON: Yes.

COMMISSIONER GRANT: Have you the figures on the percentage of the total personal income tax that is paid by taxpayers in the various income ranges?

MR. MAGNUSON: Well, not up to date. I have some in a partial sense. In this brief, for example, we have these figures.

COMMISSIONER GRANT: Which brief is that?

MR. MAGNUSON: The brief to the Sirois Commission.

COMMISSIONER GRANT: In 1937?

MR. MAGNUSON: Yes. We have the brief that was submitted to the Gordon Commission in the 1950's. As far as a worker with an average family is concerned, I have some figures that show that the income tax alone for an average family with two children with an income of below $5,000.00 amounts to roughly 7% of his income. The rest is indirect taxation.

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THE CHAIRMAN: There is one point here I would like to go into further. Paragraph 33 on page 8 suggests that the increase in the basic income tax exemption for single persons to $2,000.00 and for married persons $3,000.00. I think we all agree with you that taxes should not be collected from people that don't have enough to live on. It is a difficult thing to measure. There have been surveys as to where, if you like, the poverty level may lie, the sustenance level. Do you have any such survey? Where do you come by your figures of two and three thousand dollars?

MR. MAGNUSON: Well, we haven't a survey. We haven't made any such surveys. There are surveys which we have looked at which have been made by welfare agencies and various organizations which show what it takes as an average today to live on. That is, what is needed to meet a reasonable amount of expenditures. They certainly do come far above the amount that is allowed here. This is very conservative. I would say they should be higher, the exemptions should be higher. Speaking about this, I would think it a very conservative figure.

THE CHAIRMAN: Could you give me a reference to a Canadian survey which would be useful in this matter?

MR. MAGNUSON: The Ontario Welfare Council for one.

THE CHAIRMAN: We need one for all of Canada.

MR. MAGNUSON: I can't think of any name. I know that there are such. I don't know if I have any.

THE CHAIRMAN: Recently somebody appearing before us made reference to a United States study which obviously

had some validity, but I would prefer here a Canadian study.

MR. MAGNUSON: Was that the Hellyer Study?

THE CHAIRMAN: I think not.

MR. DEWHURST: I think the Ontario survey takes comparative figures from across the country, not only related to Ontario.

THE CHAIRMAN: That is the Ontario Welfare Council, 1941?

MR. MAGNUSON: Yes, that is right. I thought I had here in an old information service bulletin some references, but it is not here. I must have it in some other reference book I didn't bring with me. For instance, there is a research bureau on the west coast that has conducted a number of surveys at times in a limited area across the country bearing on this point and that might be helpful. Then, of course, there is the Hellyer budget. In California there is an organization that is referred to. The Canadian Labour Congress, the old Trades and Labour Congress of Canada, did publish a bulletin some years ago which had some statistics on this based on an impartial survey that was carried out across the country. That was during the war time. It applied to the cost of living at that time and the requirements when P.C. 103 came into being just about that time. I am sorry I cannot state the exact number of this bulletin or the date it was issued.

THE CHAIRMAN: We can find that out. I think we have no more questions. Have you anything further you would like to say to us?

MR. MAGNUSON: Well, that is all.

THE CHAIRMAN: We thank you very much indeed for your submission to us, and your appearance here today. None of us like taxes and I would suspect, in view of the philosophy of your party, you like them even less than the rest of us. In view of that it is very good of you to take the time and trouble to come before us.

MR. MAGNUSON: I shall be very happy if I find anything that bears on the point you raised to mail it to you, any written document that bears on taxation.

THE CHAIRMAN: Well, I would certainly like to read it providing it is in English. I couldn't go very far beyond that.

MR. MAGNUSON: Yes, of course.

THE CHAIRMAN: Thank you. We will stand over for ten minutes.

---Short Recess.

F/ET/dpw

THE CHAIRMAN: Mr. Secretary, are we ready?

THE SECRETARY: Mr. Chairman and Commissioners, we have this morning with us Mr. L.C. Foster and Miss Ursula Foster. Mr. Foster has presented a brief to the Royal Commission which you have before you, and he wishes to speak to this brief this morning. I would like to enter it into the records as Exhibit No. 81.

--- EXHIBIT NO. 81: Submission of Mr. L.C. Foster.

THE CHAIRMAN: Thank you, Mr. Secretary. Good morning, Miss Foster and Mr. Foster. Thank you, indeed, for your submission. I might say this gives me some personal satisfaction because I have been of a little assistance at one time in guiding Miss Foster's steps in income taxation; perhaps not very far, but a little bit, and I see that she has picked up anything I said to her and I think a great deal more in this submission.

Mr. Foster, there is no need to read your brief to us. We have already read it. Most people appearing like to speak to what they have sent in by way of summary or additions to it or anything that they please, and we will be very glad to hear anything you have to say. Otherwise, we will have a few questions to put to you.

MR. FOSTER: I would like to say, firstly, that, oddly enough, we are not seeking relief from taxes. We are seeking more - and I should have written the words out to get this more clearly - we are seeking more to have a more economic approach by the Tax Department and a fairer approach by the Tax Department. If I may read

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just this summary.

THE CHAIRMAN: By all means.

MR. FOSTER: My submission outlines some undemocratic and very unfair features in the operation of the Income Tax Department, as far as the small taxpayer is concerned.

The small businessman is very vulnerable because he usually does not have the time or resources to contest decisions. If the amount is small, the Income Tax Department assumes he will not contest a decision of even a junior assessor as the cost of auditor and/or legal fees would be greater than the tax. Legal fees thus incurred would not be allowed as an expense.

When an objection to a re-assessment is filed, the whole file is opened, and decisions that have already been made are subject to reversal. My sister's status as a tenant could be reversed and she would have to pay back taxes and penalties. At the same time, I would receive a tax rebate with interest. This sort of thing no doubt keeps assessors busy, as the Department can go back four years and three or four assessors can screen it (the file) in that time.

In court, when an accused person appeals, only the item under appeal can be considered, and during the appeal he cannot be threatened with other charges. This sort of justice does not apply in the Income Tax Department.

THE CHAIRMAN: Now, Mr. Foster, you are an engineer, I see, a professional engineer in the Province of Ontario?

MR. FOSTER: Yes.

THE CHAIRMAN: Employed by Dearborn Chemical, and your interest in taxation comes about because of taxes that you are paying yourself, I think?

MR. FOSTER: Yes, that is correct. Excuse me, sir; my experience, just very briefly: I graduated in 1938, and my industrial experience was varied until about 1952, and then, for 5½ years, I was manager of a small chemical company, and we struggled, and then there was a change of ownership which let me out. Then I struck out as an independent sales agent sort of on a catch-as-catch-can basis. Then, at the beginning of last year, I joined the Dearborn Chemical Company in the service department as a regular employee. So I only say those words to indicate that I have rather a vivid picture of what the small businessman has to contend with.

THE CHAIRMAN: You have put quite a few recommendations before us. I think I have counted seven in all. Are there any questions?

COMMISSIONER MILNE: I would like to ask you a question just to clear up in my own mind the facts that surround this particular case. I gathered from your submission you have this apartment as an investment, and I have no idea how long it has been an investment in your hands. You mentioned that the original refrigeration system had never been capitalized.

Am I right in assuming, when you bought this apartment, or purchased it, or in whatever manner, that the refrigeration system as it exists now was in the building at that time?

MR. FOSTER: Yes. My sister, in her letter,

4 outlined the details. I believe it was 1957 that my father died. Actually, he had had his house in the city converted - it is an old house, and it was converted into three apartments in 1944. My sister and myself took over this building, and in 1944 the refrigeration system was installed with a compressor in the basement and three boxes.

In this particular instance, we found we could not get an exact unit to replace them, but as you suggested, originally the refrigeration system was not separated from the building as a whole. It was just considered that, and we felt that it was just a replacement of a certain item. In the course of this certain principles seem to come out. One of the main principles, as I see it, is that in one way or another these refrigerators happen to be an expense. Whether they are taken in one year or over a period of years depends on the Tax Department.

Now, to us it seems a waste - and we are not trying to dodge it, you see - but to us it seems a waste of assessors' time and therefore taxpayers' time to capitalize an item worth $170. That may have been all right in the 1930's, but aside from the fact that it was a unit, you might say a unit that was already in the house, and capitalized with the house, there is this uneconomic feature.

Then, of course, the additional unfair approach of which this is just an example.

I know, from talking to accountants who deal with small business firms, that this is a regular practice.

5 When you appeal one item your whole file is opened, and we were put in the unfortunate spot in this particular item, that the choice, as I outlined, was given to me: "We will close your 1961 file if you unconditionally withdraw your objections."

Well, this is sort of like "When are you going to stop beating your wife?" because do not have anything to hide. But then we just did not feel that we had the time and energy and so forth to go into a long fight on a bunch of other items that these people would bring up. Have I gone farther than your original question?

COMMISSIONER MILNE: That is all right. You certainly cleared the point for me. I wanted to ask you one other thing in connection with your submission which you show as your first recommendation. It deals with Section 51 and the time in which additional tax must be paid. You do not think it should be necessary to pay this within 30 days? Did you have a definite time limit that you would suggest?

MR. FOSTER: I suggested that at the end of the appeals - that could vary.

COMMISSIONER MILNE: Yes.

MR. FOSTER: Within 30 days. Payment of additional taxes due to re-assessment should be required only after appeal and/or objection has been settled.

COMMISSIONER MILNE: You thought it should go on even though this could be a very lengthy period?

MR. FOSTER: Yes.

THE CHAIRMAN: Well, it is very good, indeed, to

have this directed at assessing tax. Most of what we have received, of course, is directed at the economics of taxation or the language of the Act. We do hear a bit about the assessing practice, but not a great deal, and we are delighted to receive a submission from an individual taxpayer who is particularly concerned about the way the Department proceeds to assess.

You may be sure we will continue to examine this, and if there are matters which can be corrected, we will give them our attention. I think we have no more questions. Is there anything further you would like to say to us, Mr. Foster or Miss Foster?

MISS FOSTER: There is one item from my own company, the Wholesale Diamond Merchants. We have very heavy sales and excise taxes, more so than corporate income taxes, and, of course, the auditors come in periodically. They never clear up to a certain point, say, 1960. They will clear up certain items to 1960 and two years later they will come in and dig up 1956 or 1955 or 1954.

Then, what we have been doing in all good faith, they will say, "No, that is not so," so then we have a little penalty. Not much.

However, if only they would clear the decks to a certain point that you would know where you are at once it is audited. The private auditors from an auditing firm do the audit for a year - unless, of course, there is a suspicion of fraud, then I realize they would have to go back then, but if they could clear the decks to a certain definite point on each audit.

7 THE CHAIRMAN: Thank you, Miss Foster. You have put it on the record. You might find it useful to address yourself by letter to the responsible department. However, in all events we will have regard to the matter, I can assure you.

2 Thank you very much indeed for your appearance here today and your help to us.

MR. FOSTER: This same sort of thing applies even in very small items. Real estate. We can never really be sure that we are cleared up in any particular period. You know, four years back, and we are always open for more. Thank you very much indeed for taking the time.

THE CHAIRMAN: Not at all. We are glad to see you. Thank you.

Mr. Secretary, what is next?

THE SECRETARY: I have one more item of business, Mr. Chairman. I have a brief submitted to the Commission that was received on April 16th in Ottawa from the Rubber Association of Canada. I understand that Association will be appearing before the Commission some time in the autumn in Ottawa. At this time, with the concurrence of the Secretary of the Rubber Association of Canada, I would like to enter this brief into the record as Exhibit No. 82.

THE CHAIRMAN: Thank you, Mr. Secretary.

--- EXHIBIT NO. 82: Submission of the Rubber Association of Canada.

8

THE SECRETARY: There is no further business, Mr. Chairman, in Toronto. We will be meeting in Ottawa at 9.30 on Monday morning at the Board of Transport Commissioners.

THE CHAIRMAN: This completes the Toronto submissions. We stand over now until 9.30 on Monday morning in Ottawa. This hearing is concluded.

--- Adjournment

ROYAL COMMISSION

ON

TAXATION

HEARINGS

HELD AT

OTTAWA
ONT.

VOLUME No.: 27

DATE: MAY 27, 1963

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ROYAL COMMISSION ON TAXATION

Hearing held in the Board of Transport Commissioners Hearing Room, Ottawa, Ontario, on Monday, the 27th day of May, 1963.

COMMISSION:

MR. KENNETH LeM. CARTER -- Chairman

MR. J. HARVEY PERRY

MR. A. EMILE BEAUVAIS

MR. DONALD G. GRANT

MRS. S.M. MILNE

MR. CHARLES E.S. WALLS

LEGAL ADVISER:

MR. J.L. STEWART, Q.C.

RESEARCH DIRECTOR:

PROF. D.G. HARTLE

SECRETARY:

MR. G.L. BENNETT

ROYAL COMMISSION ON TAXATION

HEARINGS HELD AT THE CITY OF OTTAWA, ONTARIO

May 27, 1963

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Ottawa, Ontario,
Monday,
May 27th, 1963.

---The hearing commenced at 9.30 a.m.

THE CHAIRMAN: Would the Secretary introduce our visitors to us?

THE SECRETARY: Mr. Chairman and Commissioners, this morning we have a brief from the Professional Institute of the Public Service of Canada. Dr.B. Coldwell is the vice-president of the Institute. He is here to speak to the brief, and with him, two colleagues, officers of the Institute. I would like to enter this brief into the record as Exhibit 83.

---EXHIBIT NO. 83: Brief of the Professional Institute of the Public Service of Canada.

SUBMISSION OF THE
PROFESSIONAL INSTITUTE OF THE
PUBLIC SERVICE OF CANADA

APPEARANCES:

Dr. B. Coldwell
Mr. J.H. Leroux
Mr. F.S. Morris

THE CHAIRMAN: Thank you, Mr. Secretary. Good morning, Dr. Coldwell. I would like you to be so kind as to introduce your colleagues. I will introduce the Commission. I do not need to name them as their names are up here. If you would care to speak to your submission, please do so. We have all read it. It does not need to be read into the record or to us. It is in the record now, but if you have anything you would like to add or summarize we would be very glad to hear anything you have to say.

DR. COLDWELL: Mr. Chairman and Commissioners: I would like to introduce Mr. Hector

Leroux on my right, our executive secretary, and Mr. Morris on my left, who is a member of our legal group. We are appearing here this morning on behalf of our President, Mr. Gilhooley, who was unable to come.

I think I should point out that the Professional Institute of the Public Service of Canada is a staff association which represents professionals in the public service.

THE CHAIRMAN: The acoustics in this room are dreadful. Will you raise your voice a little bit, please?

DR. COLDWELL: I should point out that the Professional Institute of the Public Service of Canada is the voice of professionals in the public service, and we have a membership of approximately 6,500 at the moment. The brief makes four recommendations. They are before you. I do not think I have anything further to add to this at this time. We will try to answer any questions you may wish to put to us.

THE CHAIRMAN: Thank you, Dr. Coldwell. You may remain seated. In the Professional Institute of the Public Service whom do you classify as professionals? I presume it would be doctors, lawyers, engineers, accountants.

MR. LEROUX: There would be chemists, bacteriologists, biologists, pharmacists, nurses, and generally speaking those who are university graduates who are employed in the federal public service in these

categories.

THE CHAIRMAN: There are a few left over who do not qualify.

MR. LEROUX: Well, we would include such people, for example, as administrative officers, personnel officers, and other related fields in management, in the management areas.

THE CHAIRMAN: Do you have a committee on taxation? I was wondering how it is that you come to submit a brief to us. Did you make studies of tax laws?

DR. COLDWELL: We have a committee on superannuation and insurance, and we have a committee on legislation. These are standing committees of our organization, and these committees on occasion, as the occasion demands, do make studies on legislation and tax laws.

THE CHAIRMAN: Thank you. I might say we are very glad to have this submission. We feel it is an important one. We will have a few questions for you.

COMMISSIONER GRANT: It is Dr. Coldwell, is it?

DR. COLDWELL: Yes, that is correct.

COMMISSIONER GRANT: If I understand your brief correctly, you are restricing your comments largely to the position of the widow and children.

DR. COLDWELL: That is right.

COMMISSIONER GRANT: Of the deceased person. Your first submission is that the family home should be regarded as belonging to the husband and

wife jointly or with a minimum amount of $10,000 being the dividing point.

DR. COLDWELL: That is right.

COMMISSIONER GRANT: Now, you are aware of course, of the provisions of the gift tax section of the Income Tax Act, which is Section 112, and I thought we might just review some of the provisions which already exist in the light of your submission.

I think you make a point that while relief is available, already available, that it could only be taken advantage of if the person knows the law. I think you make a point it is not always easy to find out what the law is.

DR. COLDWELL: That is right.

COMMISSIONER GRANT: The Gift Tax Act already provides that a husband can deed his residence to his wife, and on his death $10,000 of that valuation of the residence will be exempt from being included in the value of the residence. That provision already exists in the Income Tax Act.

Also under the gift tax provision, a person can gift up to $4,000 in one year to one person, or one-half of his taxable income of the previous year, whichever is the greater, so that a measure of relief does exist under the Income Tax Act there. Perhaps it is well for us to keep these in mind, you would agree, in considering any amendments to the Estate Tax Act.

Now, there are two provisions of the Ontario Succession Duty Act which you draw to our attention. They seem to be provisions which are

working quite well in Ontario, and naturally they will have full consideration of this Commission.

There is a further provision in the Estate Tax Act that in the event of property being held in joint tenancy, on the death of one spouse, the actual interest of that spouse will be included in his or her estate, but no more.

Now, those are about the only observations I have to make. Perhaps you might have some further remarks in enlargement of your brief in the light of those observations.

DR. COLDWELL: I will ask Mr. Morris to comment on your observations, Mr. Grant.

MR. MORRIS: Mr. Chairman, gentlemen, firstly, the Professional Institute are well aware of the provisions of the Gift Tax Act and Section 112 of the Act. However, the Institute feels that the man on the street, he is unaware of the provisions of the Gift Tax Act. Furthermore, the section is not too explicit. The exemption must be claimed, and if not claimed, of course there is no presumption on behalf of the widow.

Furthermore, with respect to the annual gifting, the amount of $4,000, of course this is a section which more readily applies to the well-to-do and the wealthy in this country. In that connection we feel that the average Canadian is more or less discriminated against. We think that the provisions of the Statute itself, the Estate Tax Act, based on federal authority and the Succession Duty Act in the

Province of Ontario, should spell out clearly the exemptions and other provisons that are available to the average Canadian.

It is quite clear that since commuted pensions and annuity rights are taxed on a commuted basis, this fact alone is placing many estates into the tax bracket. The average Canadian is completely unaware that his estate may be taxable.

In fact it is quite clear that even solicitors of the Department of National Revenue are not clear as to what the law is today. We have a rather anomalous situation of a senior solicitor of that Department soliciting estate planning advice from a junior insurance man. That to my mind is a grave indictment on the Act itself. Here is a man supposed to be an expert in his field. While it is true that possibly he is terrified by the knowledge that he possesses, I personally am aware that recently a senior solicitor of that Department solicited estate planning advice from a very junior insurance salesman who was taking a correspondence course leading to the so-called degree of C.L.U.

COMMISSIONER GRANT: Estate planning is becoming a more and more complex problem. It might be a very foolish man who would think that he had all the answers himself and could not profit by taking advice. However, you know of the particular instance which we will not go into.

The provision with respect to the capitalization of annuity or pension has been brought

to the attention of the Commission on several occasions in previous hearings, and I am sure what you have to say will be taken into consideration very seriously along with the approaches which were made by other organizaions.

It has been brought very forcibly to our attention that there are instances where capitilization of life interest does work a considerable hardship where liquid funds are not available and where the income may be subject to quite severe strain in order to find the funds with which to pay the estate duty.

MR. MORRIS: I might say that the Institute in the month of March presented several recommendations to the Premier of this Province. These recommendations were well received, and we have received a reply to the effect that possibly the Institute may be suitably impressed by amendments to existing legislation in the Province.

COMMISSIONER MILNE: May I ask you about the amount of $10,000? I think you are thinking in terms of income, as you phrase it, of moderate means, and I was wondering if you would tell us why you picked that particular amount. Is it because that is the amount mentioned in the gift tax or were there some other conclusions that you reached to take ~~that~~ this amount, "one-half or at least $10,000".

DR. COLDWELL: I think, Mrs. Milne, that our thinking with respect to this sum was this seemed to be a reasonable figure; that the homes of the

average professional in the public service would probably contain somewhere around this amount, this value of furnishings, and we felt that this was reasonable in that respect and that we were not asking for the moon. This seemed to be a reasonable figure. I suppose I could ask $12,000 or $15,000 or some other figure, but this seemed to be fairly reasonable.

I should point out that we are simply asking that these recommendations be studied by the Commission, and from your sources of information you might find this figure might need to be adjusted.

COMMISSIONER MILNE: You have no definite conviction about the amount? It is just that it should be a reasonable amount?

DR. COLDWELL: Yes.

COMMISSIONER MILNE: Perhaps you have already answered then the question as to what size the estate would be of a person in moderate means. You possibly feel that this would come in the same type of income?

DR. COLDWELL: Of course the size of the estate will vary considerably depending on the earnings of the individual and the time of death. A large part of it no doubt will be tied up in annuity benefits from superannuation. That, plus his home, furnishings and life insurance. Those would be the three main parts of a professional's estate. We feel in many instances it could well exceed $60,000.

THE CHAIRMAN: You have no comment on the $60,000, have you?

DR. COLDWELL: No, I don't think so, Mr. Chairman.

THE CHAIRMAN: It is not in your submission.

COMMISSIONER WALLS: I was rather glad to hear you had made a presentation to the provincial government, but it seems to me some of the problems that you have are rather aimed at Provincial Succession Duty instead of Federal Estate Tax. You must keep in mind that the Federal Estate Tax is only interested in what the deceased leaves, and not to whom he leaves it.

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The fact you get $60,000 deduction for a wife is a normal deduction, just like an income tax deduction. The wife may be left nothing by the estate and the man still gets $60,000 deduction; whereas the Provincial Succession Duty Act taxes what each beneficiary receives, therefore it seems to me more of your questions are geared to that.

Do you think it is possible, or do you see any advantage to both these taxes being collected by the one medium in the provinces where the have a succession duty?

MR. MORRIS: Could you rephrase that question again?

COMMISSIONER WALLS: Do you see any advantage to both these taxes being combined or collected by the one medium?

MR. MORRIS: Personally I think it would be far more efficient and businesslike for one authority to collect both taxes, however there is the question of provincial autonomy and I doubt if Queen's Park would look upon that with any great favour.

COMMISSIONER WALLS: I see a great deal of merit in the things you suggest, like the furniture. It seems to me you are getting away from the spirit of the Estate Tax. I am not saying that the spirit is right or wrong but there is the fact it is only interested in the total estate the deceased leaves and not who gets it. Therefore if you had a combined tax you would be better able to look after some of the problems that you are proposing today.

MR. MORRIS: Well, since we have made complementary recommendations to both authorities we feel, providing both authorities lend a favourable ear, certainly this matter can be ironed out. We feel the request is reasonable and we think it is what any widow is entitled to.

COMMISSIONER BEAUVAIS: I would like to go back to that question of $10,000. You say that you are aware of the tax provision in connection with a gift of $10,000 on property during a taxpayer's lifetime. If a taxpayer has given to his wife $10,000 of property would this suggestion apply also?

MR. MORRIS: We of course don't mean to duplicate the provision so the wife is able to collect from both sources. We are suggesting that in all the circumstances the wife should be deemed to have this equity in her family home whether or not her husband was aware of the provisions of Section 112 and took advantage of that.

COMMISSIONER BEAUVAIS: If the husband took advantage then there would be no duplication of the $10,000.

MR. MORRIS: I feel that if the amendment we are suggesting here were adopted it would lead to a deletion of a part of Section 112 of the Gift Tax Act.

COMMISSIONER BEAUVAIS: Now in the next paragraph you suggest in all circumstances all normal household appliances, furniture, and furnishings shall be deemed to be the property of the widow. Would you include in that art objects and paintings and

sculptures and so forth?

MR. MORRIS: We, of course, had this in mind. It is a matter of statutory interpretation. We would certainly not so intend -- these are not normal.

COMMISSIONER BEAUVAIS: But if it is the wife who dies first then would the same application be made? Would it be the widower?

MR. MORRIS: The Institute feels it is the widow who needs protection. Surely the widower can fend for himself.

COMMISSIONER PERRY: As I read your recommendation it is really a suggestion that the exemption of an estate be increased by $10,000 where there is a residence among the assets. Put that way I then asked myself, "What is the equity in such a provision?". Take the instance of a couple who have retired for some time and, as many of them do, sell the family home and move into an apartment. What is the equity of giving an exemption where the residence has been retained, as opposed to the situation where it has not been retained, where it has been sold and the money perhaps invested in securities or some other form of asset? Do you have any thoughts on that particular aspect? I can see how you arrived at this recommendation but I am wondering whether you had thought of it in those terms.

MR. MORRIS: We feel that the women in this country feel and believe that they are entitled to an equity in the home.

COMMISSIONER PERRY: But is it not true a lot of women in the country in advancing years do not want to be bothered with keeping up a larger home and they would rather be living in more convenient circumstances?

MR. MORRIS: I suggest that that is neither here nor there. We are primarily interested in the widow with minor children.

COMMISSIONER PERRY: Well, I must say that rather changes the brief because this widow, if she has enough minor children, would have an exemption of eighty, ninety, or a hundred thousand dollars and therefore she may not have a problem.

MR. MORRIS: Under the present provisions of the Estate Tax Act I suggest that it would be very easy to have an estate of $100,000 although you may not even be able to purchase a used second-hand car. $100,000 at five per cent gives a salary of $5,000. A widow today with an average family would have rather tough sledding on $5,000.

COMMISSIONER PERRY: Is it actual experience that there are numbers of people leaving estates valued at more than $90,000 or $100,000? I am just looking for information here.

MR. MORRIS: I have no actual figures on the matter, Mr. Perry, but I suggest that under the present provisions of the Estate Tax Act that it is very easy to leave an estate of $100,000, even though you have few visible and tangible assets.

DR. COLDWELL: Mr. Perry, when you

mentioned the case where the family home is disposed of and the family have moved into an apartment, at the time of the liquidation of the family home could not at that time the wife's equity be established?

COMMISSIONER PERRY: It would have to be established in whatever assets replaced the family home in the husband's property and once you start along this sort of line I think the effect of what you are asking is an increase of $10,000 in the basic exemption because it would almost become too complicated to do anything else.

THE CHAIRMAN: This is not the place to argue with a fellow Commissioner! I would like to ask Mr. Perry if in fact we have not started on the road in view of the special treatment given to the home in the Gift Tax sections and if that is so the arguments made are valid to the effect these gentlemen would like to have the same treatment in the Estate Tax Act as is afforded under Section 112 of the Income Tax Act.

COMMISSIONER PERRY: I suffer under the disadvantage of knowing why that provision went into the Act. It is not much of a secret; I think it was largely a recognition of the fact that a good many husbands unconsciously had made gifts of a part of their residence to their wives through entering into a joint mortgage or title. This has become very common, a good many mortgage companies insist on it. The Department was faced with the fact that perhaps hundreds of thousands of husbands all over the country

who had made gifts but had to be assessed for gift tax or removed from this position by some device, such as this $10,000 exemption.

As I said I can see the road by which they had arrived at this position which, of course, is the $10,000 exemption from the Gift Tax. This is a real argument that always comes up in the case of pensions where other testators have created other assets in other forms, a formation which just happened not to be pensions.

MR. LEROUX: I think I might suggest there is a little more than the purely financial interest here. I think there is something of the psychological interest on the part of the wife who feels a sort of proprietorship tuward the furnishings and so on.

COMMISSIONER PERRY: You can appreciate, of course, that the furniture would go with her to any type of abode. That is all I want to say, Mr. Chairman.

THE CHAIRMAN: Thank you.

COMMISSIONER BEAUVAIS: I have another question. Have you given any thought to the taxation of the capitalization of the pension when it is on a joint survivorship basis? It seems to me it is a very serious matter because the assets of a taxpayer on his death might be only the pension that his wife would receive and if this pension is capitalized then the wife will have no money to pay for that capitalized value.

MR. LEROUX: I might say, Mr. Beauvais, we have had one or two examples amongst the membership who have been obliged to use their entire proceeds of their husband's life insurance in order to pay the estate tax and succession duty charges.

COMMISSIONER BEAUVAIS: I understand that in the United States the value on which it is taxed is on the basis of the contribution of the taxpayer but otherwise it is not taxable.

THE CHAIRMAN: That concludes our questions. Do you have any others you would like to put to us, any further remarks to make?

MR. MORRIS: I might just remark, Mr. Chairman, the legal precedence under the Estate Tax Act and even under the various Succession Duty Acts are rather meagre. I think a study of the results of the report would rather clearly indicate that the Department of National Revenue normally has its way and it is quite clear that these Acts are framed in very general terminology, almost all-embracing, and we feel that this works certainly to the detriment of the average Canadian taxpayer, the man on the street. We of the Institute feel that the average Canadian is more or less inured to the high taxation under the provisions of the Income Tax Act but we feel that it is going a little bit too far to pursue the average man beyond the grave. Surely there should be some respite somewhere.

THE CHAIRMAN: Your statement as to the language of the Act is an interesting one. The reverse

is usually stated with reference to the Income Tax Act and it has been suggested that perhaps it seeks to create too great a degree of precision in its statements. Maybe there is a happy middle ground. I don't know.

MR. MORRIS: I am afraid my legal confreres with the Department of National Revenue are experts in their field on behalf of the government and seemingly the shoe is on the other foot when they think of their own future estate.

DR. COLDWELL: I would like to thank you very much, Mr. Chairman, for permitting us to appear this morning on behalf of the Professional Institute of the Public Service of Canada.

THE CHAIRMAN: We thank you very much indeed for coming forward with this interesting submission and answering our questions. We are very glad to see you. Thank you.

THE SECRETARY: Mr. Chairman, we have a brief submitted by Mrs. Denise C. Brown of Ottawa. Mrs. Brown is here before you this morning and wishes to say a few words and she is presenting this brief on behalf of herself.

I would like to enter this brief into the record as Exhibit No. 84.

THE CHAIRMAN: Thank you, Mr. Secretary.

---EXHIBIT NO. 84: Brief submitted by Mrs.Denise C. Brown, Ottawa.

SUBMISSION OF
MRS. DENISE C. BROWN, OTTAWA

THE CHAIRMAN: Good morning, Mrs. Brown, We have your submission and it is indeed very clear. I think we may have a few questions to put to you.

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I was curious as to what your professional qualifications are. It seems to be very well drawn. You are not a lawyer?

MRS. BROWN: No.

THE CHAIRMAN: You are really making a submission which is in your own interest?

MRS. BROWN: Yes, very definitely.

THE CHAIRMAN: Do you have anything you would like to say to us in amplification of your recommendation?

MRS. BROWN: No, I believe it is all contained in the submission. I will be pleased to reply to any questions that are asked.

THE CHAIRMAN: It was very well stated in your proposal that natural mothers, irrespective of marital status, be granted a basic and permanent exemption for income tax purposes of $10,000 annually, and that such exemption be made retroactive to January 1, 1957. The rectroactive feature is one that would not find much favour with the government I would think. Retroactive legislation, as you are probably well aware, in the tax area is very difficult to deal with.

We were curious as to why $10,000. Surely equity would be achieved if the natural mother were placed in the same category as a widow with a child. Would that not be right?

MRS. BROWN: Well, of course, a widow with a child, I would include that as a natural mother. By "natural mother" I meant the mother of a

child as opposed to one of an adopted child.

THE CHAIRMAN: I see.

MRS. BROWN: Rather than either a single or married woman or widow.

THE CHAIRMAN: A widow with a child in a self-contained domestic establishment now gets $2,000 I think.

MRS. BROWN: Yes, or a woman who is separated from her husband and has a dependent child also gets $2,000. In my opinion that is not sufficient. I am in those circumstances, and in my opinion the exemption equivalent to that of a married man is not realistic, as I have pointed out in the brief.

COMMISSIONER WALLS: The only thing that rather disturbed me, and I have a good deal of sympathy for a great many of the points in your brief, but I came to the conclusion that it would perhaps be unfair for a $10,000 exemption to a married woman with a dependent while a married man with two children getting $10,000 a year has to pay over $1,500 tax. Why would you state that a woman should have complete exemption of $10,000 as against the husband having to support a wife and two children and having to pay $1,500 tax?

MRS. BROWN: In the first place I mentioned the $10,000 to give the government some room to downgrade it. I think that if the government approved of an exemption of $5,000 I would be quite satisfied.

COMMISSIONER WALLS: You were carrying on a Dutch option, were you?

MRS. BROWN: Yes. The second part of your question is that from the point of view of a woman who is separated and supporting a dependent child and does not have the services of a male person in the home, it is a little difficult to understand that a married man is supporting a wife. In actual practice a married man could be requested to add to his income the value of the services of a domestic servant without pay, which is the status of a married woman in Ontario.

I wash my own dishes, but the married man next door does not wash his own dishes. He does not prepare his own meals. He has a domestic servant without pay to do these things for him.

COMMISSIONER WALLS: Some of us married men still have to wash dishes. Why did you pick on the retroactive date of 1957? Why did you particularly pick 1957?

MRS. BROWN: Because I was married in 1939 and I was under the impression, as many married women are in Ontario, that a married man is responsible for their support. It was very rudely brought to me in the Family Court and in the Supreme Court of Ontario that this is not the case. This is false.

COMMISSIONER WALLS: Your picking 1957 is to apply to your own particular circumstances? That is why you picked 1957, to make it retroactive to 1957?

MRS. BROWN: Yes. I feel I have suffered considerable injustice, and before that it

could be said that I was going under the misapprehension that my husband was responsible for my support, which he was not, and neither is any other married man.

COMMISSIONER WALLS: Thank you very much.

COMMISSIONER MILNE: It would seem if the $10,000 exemption were granted it would be much better for a woman to be a widow.

MRS. BROWN: I'm sorry. You mean it would be more advantageous for a woman to be a widow than to be a married woman?

COMMISSIONER MILNE: Yes.

MRS. BROWN: I agree with you, and when I separated from my husband I was able to claim married exemption, whereas when I was living in the same house as he was I was not able to claim that married exemption. The moment I left with my dependent child, I maintained a separate establishment three streets from my previous residence, and I immediately qualified for $2,000 exemption, so it was to my advantage, I agree with you.

THE CHAIRMAN: I believe that completes our questions, Mrs. Brown. I think we understand what you have put before us, and I assure you we will consider it. Is there anything further you would like to say to us?

MRS. BROWN: No, I do not think so, thank you.

THE CHAIRMAN: We thank you very much indeed for your attendance here today and your

submission to us.

MRS. BROWN: Thank you.

THE CHAIRMAN: Mr. Secretary, is there anything else this morning?

THE SECRETARY: One short item of business, Mr. Chairman. I have received a very short brief from the Agricultural Institute of Canada which I would like to enter into the record as Exhibit 85. The Agricultural Institute points out it is a national association representing over 3,000 professional agriculturists in Canada. By the nature of the industry the profession serves between 80 and 90 per cent of the members who are salaried employees. The conclusion: "We have been permitted to examine the submission to your Commission made by the Canadian Association of University Teachers. We should like to place on record with you our profession's complete endorsation of the principles underlying the recommendations of the C.A.U.T.". You will recall, sir, we had this brief in the City of Montreal.

THE CHAIRMAN: They spoke about refresher courses, and these are the farmers' organizations?

THE SECRETARY: Agricultural Institute of Canada.

THE SECRETARY: There will be distribution made in the usual way, but I am entering this into the record now.

---EXHIBIT NO. 85: Brief of the Agricultural Institute of Canada.

SUBMISSION OF THE
AGRICULTURAL INSTITUTE OF CANADA

Suite 100, 176 Gloucester St.,
Ottawa 4, Canada.

May 15, 1963.

Mr. Kenneth LeM. Carter,
Chairman,
Royal Commission on Taxation,
Room 1014,
88 Metcalfe Street,
Ottawa, Ontario.

Dear Sir:

The Agricultural Institute of Canada is a national association comprised of and representing over 3000 professional agriculturists in Canada. By the nature of the industry our profession serves in this country, between 80 and 90 per cent of our members must be and are salaried employees. They are employed by others to serve the industry rather than being practitioners of the profession as independent individuals or through professional partnerships.

The fact that these individuals are employed rather than self-employed in no way reduces their personal responsibility to maintain and improve their professional competence. Some employers support some of their activities and needs in these respects, but to an increasing degree, the individual is required to personally accept the responsibility. Our concern is that the Canadian Income Tax Act in its present form seriously discriminates against

salaried professionals by not allowing as deductions from taxable income the expenses which they must incur to continue to be professionally competent.

We wish to make it clear that our comments are intended to refer to all professional agriculturists whose principal source of income is from salaried employment regardless of their employer. The basic principles of the problem and its solution apply without exception in all instances where the salaried professional has to finance these expenditures himself.

We have been permitted to examine the submission to your Commission made by the Canadian Association of University Teachers. We should like to place on record with you our profession's complete endorsation of the principles underlying the recommendations of the C.A.U.T. and at the same time urge you to propose revisions to the Income Tax Act in your report that will remove the existing discrimination against salaried professionals.

Yours very truly,
J.E. McCannel, P.Ag.,
Executive Secretary.

THE SECRETARY: That is all this morning, Mr. Chairman. Tomorrow morning at 9.30 the Canadian Committee on the Status of Women, and the next following brief the Canadian Federation of University Women.

THE CHAIRMAN: Thank you, Mr.Secretary. We will stand over until 9.30 tomorrow morning.

---Adjournment.

ROYAL COMMISSION

ON

TAXATION

HEARINGS

HELD AT

OTTAWA

ONT.

VOLUME No.: 28

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ROYAL COMMISSION ON TAXATION

Hearing held in the Board of Transport Commissioners Hearing Room, Ottawa, Ontario, on Tuesday, the 28th day of May, 1963.

COMMISSION:

MR. KENNETH LeM. CARTER -- CHAIRMAN

MR. J. HARVEY PERRY

MR. A. EMILE BEAUVAIS

MR. DONALD G. GRANT

MRS. S. M. MILNE

MR. CHARLES E. S. WALLS

LEGAL ADVISER:

MR. J. L. STEWART, Q.C.

RESEARCH DIRECTOR:

PROF. D. G. HARTLE

SECRETARY:

MR. G. L. BENNETT

ADMINISTRATIVE OFFICER:

MR. A.J. SIM

ERRATA

ROYAL COMMISSION ON TAXATION

VOLUME NO. 23 - May 17th, 1963. TORONTO, ONTARIO

Page 1624, Lines 8-17 inclusive, should read:

MR. VANDERPLOEG: Mr. Chairman, I was interested in Mr. Stewart's remarks, in reading from the Radcliffe Report, about the effect of FIFO on a rising market acting as a brake on inflation because it creates more taxation and thus leaves business less money to spend unwisely. By the same token, it gives the Government more money, which it doesn't always spend too wisely. No Governments are noted for restraint in spending.

Another point he mentioned was that LIFO was fairly youthful, a fairly callow youth.

Page 1624, Lines 19-27 inclusive, should read:

MR. VANDERPLOEG: He mentioned that the LIFO system was fairly new. It is at least 30 to 40 years old. I daresay there has been more business done in the years since then than was ever done in the years all together before that. For comparison I might mention I read recently that the current U.S. budget envisions more spending than all the U.S. budgets previous, I believe, to the year 1920. While LIFO is youthful in years, it is not youthful in its application in business.

Page 1625, Lines 5-12 inclusive, should read:

MR. VANDERPLOEG: Things change, of course, and new practices have to be evolved to take care of them. I would like to mention, too, that there was a question if there had been a census on LIFO. I believe there was a study some years ago by the U.S. Chartered Accountants' Association, or whatever the name is, which approved LIFO, and it was signed, I believe, by a great many American firms in the States. Perhaps our Chairman will recall that.

Page 1625, Lines 20-30 inclusive and Page 1626, Lines 1-11 inclusive, should read:

MR. VANDERPLOEG: I recall that in our LIFO case in the Exchequer Court one of the Crown witnesses, Mr. Thompson, I believe, was opposed to LIFO - that is, his firm in Canada was opposed but his parent firm in the States was for it.

There is another point I would like to bring up, Maybe this is being a bit vindictive. Appeals to the Privy Council were abolished by Parliament in 1949, September, I believe it was, and Mr. St. Laurent, then Prime Minister, said it was a campaign issue and the country supported it. The Minister of Justice, I think it was Mr. Garson, said appeals to the Privy Council were

ERRATA (continued)

a touch of colonialism for Canada and should have been abolished long ago. I think the Prime Minister challenged Mr. Drew, then Leader of the Opposition, to say if our Courts and lawyers were not smart enough to deal with Canadian issues. Then, six years later, 1955, the same Government that abolished appeals took our case (which we had won in the Exchequer and Supreme Courts) to the Privy Council. In the intervening years, our lawyers and Courts apparently became less smart instead of smarter! To be sure, there was a hedge when abolishing appeals. Either party could take it to the Privy Council if the case was then under consideration by our Courts. Surely, however, that reservation wasn't to be invoked by the Government which had abolished appeals but was for the benefit of other aggrieved parties.

Page 1626, Lines 14-15 inclusive, should read:

MR. VANDERPLOEG: I just wanted to make these points. Thank you very much.

ROYAL COMMISSION ON TAXATION

HEARINGS HELD AT THE CITY OF OTTAWA, ONTARIO

May 28, 1963

TOPICAL INDEX — VOLUME No. 28

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the Status of Women. Volume No. 28

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Volume No. 28

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Ottawa, Ontario,
Tuesday,
May 28th, 1963.

---The hearing commenced at 9.30 a.m.

THE CHAIRMAN: Mr. Secretary, shall we proceed?

THE SECRETARY: Good morning, Mr. Chairman, Commissioners. We have this morning representatives here of the Canadian Committee on the Status of Women. This Committee submitted a brief, and the group before you this morning is led by Mrs. W. H. Gilleland, who is chairman. Mrs. Gilleland will speak to the brief. Mrs. Gilleland will also introduce her colleagues. I would like to enter this brief into the record as exhibit No. 86.

---EXHIBIT NO. 86: Brief of the Canadian Committee on the Status of Women.

SUBMISSION OF THE
CANADIAN COMMITTEE ON THE
STATUS OF WOMEN

APPEARANCES:

Mrs. W. H. Gilleland, Chairman
Mrs. Frank Flaherty
Mrs. Betty Gordon
Mrs. R. Bishop
Mrs. D. Thom

THE CHAIRMAN: Good morning, ladies. We have your submission and we have read it with considerable interest. We would like you to speak to it if you have anything you would care to say. We have all read it.

MRS. GILLELAND: Yes.

THE CHAIRMAN: You do not need to read it. Would you care to introduce your associates to us?

MRS. GILLELAND: Thank you, Mr. Carter. On my extreme right, Mrs. Frank Flaherty, press secretary, Miss Elizabeth Gordon, treasurer; next to me on my left, Mrs. Bishop, recording secretary, and Mrs. Donald Thom, corresponding secretary.

In the communications from the Secretary I gathered that you might want us to identify our organization.

THE CHAIRMAN: That is right.

MRS. GILLELAND: Now, what I have to say, there are four sentences in the opening paragraph and I cannot do it any faster or any shorter than that. Just skipping the first sentence, our attention was first concentrated on arousing in husbands and wives an awareness of the disabilities which widows suffered under the old Dominion Succession Duties Act. To accomplish this we compiled and widely distributed basic information in lay language in the belief that an informed public opinion will compel governments to amend existing out-moded legislation.

The overwhelming response and the commendation of our educational material from individual women across Canada and from national organizations, both women and men, prodded us into taking this further step: We made a number of written and oral submissions to the Federal Government throughout the progress of the Estate Tax Act from Bill 248 through the replacing bill C-37, and finally made a submission to the Senate

Committee on Banking and Commerce in 1958.

We feel that we have not only reached the man on the street, but I sometimes think we might far better say the woman on the farm because the correspondence and requests for information that have come in from local Women's Institutes all across Canada have been something that we found incredible, but certainly rewarding and stimulating and encouraging.

In our approach to you today we want to state what our approach to you is because this is a little different from the approaches to the Federal Government which we have made in the past, and when I say Federal Government, I mean Federal Liberal and Federal Conservative through the history of the legislation. We thought in our approach to the Royal Commission we had to pay attention in our own minds at least to what we have done before and in the method of approach, and in our requests over ten years we have been working on a $50,000 exemption. This was a detail, and we recognized it, so we are maintaining in our approach to you this detail only and we have moved it from a $50,000 figure, which has been partly met, of a true exemption; namely, it is $40,000 now with $60,000 true exemption for widows. We have in true feminine form made the old compromise and we are submitting a figure of $75,000 as a true exemption.

In our minds we know $50,000 is not enough and we haven't even got the $50,000 anyway. We really think it ought to be $100,000 true exemption, but being women, we have set a middle figure of $75,000 so this is

the figure we are presenting to you this morning as the proper one that our experience tells us and our philosophy tells us also is the one we had better ask for to be reasonable, and also because we think we might get it.

All our approaches in the past to Governments have been based on trying to be reasonable and asking only for what we could get. It has also been what we call the whittling approach. You take one thing and you whittle it into shape and you get a little off. In our case it is really a build-up rather than the knife-remove material. Perhaps we have been able to remove through many women's organizations some of the encrustations, or something like that, that have been in Federal legislation in the Succession Duty Act.

However, in our brief to you we are going to pass this whittling process, and we are presenting two major pieces of what we think is taxation philosophy. Our first point is the $75,000 true exemption. The second one is the recognition of the women's contribution to the marriage partnership, and I should no doubt read that to have the wording precise, but I am not going to at the present moment. We will get to it later. This is a piece of philosophy that has been presented in briefs to Government even though we did not think we had a hope of reaching through amendments to the Succession Duty Act; even though as far back as Mr. Abbott there was a statement this was to be a major overhaul. We still presented the philosophy of the recognition of the marriage partnership and the

contribution of women in it, and that means the money contribution as well as all the other kinds. There was some recognition of this in the Senate Finance Committee, but the climate at that time politically was not suitable for getting very far with the Senate at the time they sat, as between Senate and the House of Commons. That was about 1958.

Nevertheless, the Senate is a comparatively detached body, and they did pay attention to this idea, and in our presence the Commissioners debated -- I don't know if "debated" is the right word, but they debated back and forth across, and we were cross-questioned to some point, too, and it was given a good deal of thought, and they apparently did not think it was a crazy idea, let's put it that way.

Now, today in our presentation on this philosophical argument which Mrs. Flaherty is going to start with -- that is a good one! -- We feel that since this Commission is going to overhaul the whole philosophy of taxation we have a hope at least of getting this; and our last point on the delay of taxation, those two bits of philosophy will be received we know at least in the thoughtful way as it was in the Senate and we may have a hope of making a dint in the philosophy of taxation in Canada in regards to the Estate Tax Act.

Now, with those few confused remarks we will go back to the $75,000 true exemption, and Mrs. Flaherty is going to present an argument or two.

THE CHAIRMAN: Thank you, Mrs. Gilleland, for your expression of confidence in what we can do.

MRS. GILLELAND: Thank you.

THE CHAIRMAN: Mrs. Flaherty?

MRS. FLAHERTY: Mr. Chairman and Members, as you know, the figure of $50,000 is the top level of estate; all estates under $50,000 would not be taxed. This figure was set in 1941, and we all know what has happened to the value of money since that time. Yet this is the figure that still remains in the Estate Tax Act as the minimum; any estate over $50,000 comes into the estate tax picture.

We maintain that $75,000 would be a more realistic figure taking into consideration the inflated value of the dollar and the increase in all other commodities and all other expenses. The administrative costs have become terrific since many more estates now come into the tax picture. The proportion of estates in 1961 between $50,000 and $99,000 was 55.71 per cent of the total number of estates that were valued for succession duty purposes.

THE CHAIRMAN: The 55.71 per cent is what?

MRS. FLAHERTY: That is the percentage of the total number of estates that were valued for taxation, for estate tax purposes. The tax imposed on that number was only 7.7 per cent of the total revenue from estate tax, and in the over-all revenue picture in Canada the succession duty does not loom very large. It comes to about 1.5 per cent of the total revenue.

We maintain that a hardship or an imposition that brings in so little revenue is out of all

proportion to the hardship worked on a great number of people.

As I say, our basic argument is that everything is costing more and also administrative costs have gone up. When you have three or four assessors coming in to work on an estate that is just over $50,000,it becomes a very expensive item.

MRS. GILLELAND: We can say too one does not know whether to be angry because you have to pay the Federal tax assessor to assess it or whether to say it is unjust that you should be paying the Provincial assessor whose salary precumably comes out of the taxpayer's pocket.

THE CHAIRMAN: I have seen figures of the 55.71 per cent and 7.7 per cent, and the source of those I think is national tax statistics.

MRS. GILLELAND: The Dominion Bureau of Statistics.

THE CHAIRMAN: And the year is 1961.

MRS. FLAHERTY: 1961.

MRS. GILLELAND: Now then, Mrs. Gordon will begin on the argument about the recognition of the contribution of the wife to the marriage partnership for estate tax purposes. -- only, I should add.

THE CHAIRMAN: Perhaps we might take these one by one. If we have any questions we will ask them as we go along. Do you think that would be easier?

MRS. GILLELAND: Yes, all right.

COMMISSIONER MILNE: Shall I address to you the question, Mrs. Gilleland, on the $75,000 true exemption?

MRS. GILLELAND: It doesn't matter. Mrs. Flaherty will answer, and if we do not like her answer, we will add.

COMMISSIONER MILNE: It certainly has been drawn to our attention that other professional groups support this principle very thoroughly, the principle that there should be a true basic exemption. The Canadian Institute of Chartered Accountants and the Canadian Bar in their joint submission, through their joint committee, support this principle that there should be a true exemption. Their figure of course is just not a figure other than a true exemption meaning $60,000. We have some participants who have suggested larger amounts than $75,000, and some have suggested less than $75,000.

Now, was there something that we could accept as being an indicator as to how you arrive at the appropriate figure to be used? You suggest to us $75,000 is where you would like to start, yet you also mention that you really feel $10,000 should be exempt. This latter figure also has been mentioned to us.

Would you have something that would indicate to what you have geared this?

MRS. FLAHERTY: As you know, the cost of living index is based on 1949 figures as 100 per cent, and the cost of living has gone up 30 per cent.

If 1941 figures were taken, it would come to about 50 per cent. This is half way between. This is about a 50 per cent increase on the figure that seemed to be logical and did not cause too much excitement in 1941. It seemed in 1941 as if $50,000 was a reasonable figure.

Now, if $50,000 was a reasonable figure in 1941, it certainly is not a reasonable figure now, and this is an increase of 50 per cent, taking that as an indication of all the increases that have gone on.

COMMISSIONER MILNE: Yes. Then very definitely you have geared this to the cost of living?

MRS. FLAHERTY: Yes, and the inflated value and the general picture. I mean some things, as you know, have gone up more. Property values are fantastic. You cannot even predict when you leave a house to your wife, or a farm to your wife, how much that is going to amount to in your estate. It may be nothing or it may be $100,000 -- something for which you paid $4,000 or $5,000.

MRS. GILLELAND: And also I think we mention in a later connection the impact of pension schemes and capitalization thereof which we do deal with at a later point. It relates to the $75,000 figure too.

COMMISSIONER GRANT: Appropriately enough of course you are confining your representations so far as this Commission is concerned to the Estate Tax Act which is a Federal statute. Do I understand

you have looked into the Ontario Act, and have you made representations or do you intend to make representations --

MRS. GILLELAND: Present, past, and future, affirmative. Past, present and future, all affirmative.

COMMISSIONER GRANT: What is the latest submission you have made to the Provincial Government?

MRS. GILLELAND: Well, the result was in (a) the budget speech in February and (b) $60,000 exemption for widows. This is what we asked for, but we have been at that for about three years in the Provincial field and went to Mr. Frost about three years ago now with a brief and presentation. We have either the famous or infamous green sheet on Provincial succession duties even as we had an infamous at first but later famous blue sheet on Federal Dominion succession duties which just since November has been on an on-request-basis-only distribution through Ontario of over 5,000 sheets. Also a supplementary white memorandum sheet which came out between the budget speech and the Act, the amendment to the Provincial Act, alerting some of our correspondents. We hadn't had a wider coverage because we couldn't afford it. Maybe this ammouncement in the budget was going to be adequate, but we had better watch for a few things. There is no mention of any across-the-board true exemption which we have of $40,000 certainly for sure

in the Federal, and do not have in our language in the provincial, so, yes, we are concerned and alarmed.

B/MC/je

COMMISSIONER GRANT: Have you given consideration or made any representations with respect to the dual system of taxation which exists in the Estate Tax and Succession Duty field?

MRS. GILLELAND: I will have to say "no" to that. Could I give myself an excuse? When we first started with the Federal, the Ontario -- we knew there was no use going to them at that point because this was changing into the Estate Tax Act from Dominion Succession Duty to Estate Tax. That was 1959. Then it took the Ontario government a while to decide they were going to do something. We do try to pay attention to timing in submissions. Could it possibly be that we could get one assessment across Canada, one Estate Tax valuation and one Estate Tax so it would cost the same amount to die, whatever province?

COMMISSIONER GRANT: In other words, that is what you favour?

MRS. GILLELAND: Yes. Our Committee has discussed this.

COMMISSIONER GRANT: You have not included that in your presentation.

MR. GILLELAND: No, we wish we had. We have in an indirect way. Our green sheet for Ontario under the Succession Duty heading says, "It costs more to die in Ontario". So they know, people in Ontario certainly know it costs more to die in Ontario.

COMMISSIONER GRANT: Would you favour

Federal legislation with respect to Estate Tax or only Provincial legislation?

MRS. GILLELAND: No, we discussed that yesterday afternoon and we favour a Federal tax. There is a reason for that, namely it will be uniform. If the legislation is Federal, just like the Criminal Code, that is Federal and administered by the Provincial Courts, et cetera, et cetera. the same Provincial institutions. Now then, why is it not feasible, and it certainly has been feasible to have the Federal Criminal Code and have it bear a satisfactory relationship to the provinces, surely it is equally feasible and reasonable to have a Federal Estate Tax because it will be an Estate Tax if it is Federal rather than a Succession Duty and that would give this the same uniformity. Have I answered your question or not?

COMMISSIONER GRANT: I think when you draw a comparison between the Criminal Code and the Estate Tax Act you must keep in mind, must you not, that one has to do with the administration of law and the other has to do with a taxing statute?

MRS. GILLELAND: Excepting in this way -- my husband never understands why I think the way I do-- there is a parallel in my mind and it is this: As I envisage, and I think as our Committee envisages, the one tax, the Federal would levy it, I assume, but I don't know that the Federal would collect it and that the provinces would spend it.

COMMISSIONER BEAUVAIS: Just one question:

Your organization is a national one?

MRS. GILLELAND: Yes.

COMMISSIONER BEAUVAIS: Have you ever made recommendations to the Quebec Government?

MRS. GILLELAND: No, not yet but we are only ten years old, you know. There is an organization, I think there is more than one, one of the women's organizations that is working in the Province of Quebec actively. I don't know if they made a representation yet. I don't think they have. It is the Canadian Federation of University Women. The Quebec Section is very active right now and for about three years now particularly, and not just on succession duties but on all the aspects. We also think it is polite to get this done through the province.

COMMISSIONER PERRY: I find the idea of increase in exemption quite interesting. I was wondering if you have worked out the arithmetic?

MRS. GILLELAND: Not me. I can only add a bridge score. You mean cost-wise to the Government?

COMMISSIONER PERRY: The reduction in estate tax that results.

MRS. FLAHERTY: It is a very small proportion of the revenue. It would be a loss of revenue of about one and one-half per cent of the amount collected from succession duties.

COMMISSIONER PERRY: I was trying to assess the real concern of women here in facing estate tax. Obviously they are all concerned. The fact

is at $75,000 the savings from increase and exemption would be $1,800 and at $100,000 it would be $2,700. Are these the kind of amounts that concern you? They are not relatively large amounts.

MR. FLAHERTY: What we are concerned with is so many estates would not be taxed. There would be no tax on 55 per cent of estates that are now taxed, they would pay none. These are border-line estates, you know. You know how the value can come to $50,000 before you turn around. You have a house, a car, a pension. There is the $50,000, especially when the pension is capitalized. Today pensions are becoming part of the work pattern. All the advertisements you read in the paper mention pension plans. Now they are bringing in portable pensions and everyone, nearly everyone, is eventually going to be involved in the pension. People are floored when this pension is capitalized. Many women don't know this is going to happen to them. They think they have a small estate and the next thing you know there is this hefty lump.

COMMISSIONER PERRY: Is it the element of surprise or the financial burden you are concerned with?

MRS. BISHOP: I think the element of surprise has a good deal to do with it.

MRS. FLAHERTY: When these estates are being valued for taxation purposes the husband is gone. He set up his will presumably to protect his wife and children. He may not have thought -- nobody knows how

old they are going to be when they die or how old their wife is going to be when they die. This is a figure that they cannot put into their thinking when they are setting up the will. It depends on the age of the wife at the time of her husband's death because there is no account taken of whether she comes from a short-lived or long-lived family. Her age is set up by the life expectancy table.

COMMISSIONER PERRY: I am not trying to put words in your mouth or ideas in your mind but is it rather the emotional upset and the fact that the wife is completely unprepared for this?

MRS. FLAHERTY: It is the financial burden. It could happen when the children are ready for college and having to pay the Estate Tax within six months, a lump sum, it could be quite a burden if there are no liquid assets.

COMMISSIONER PERRY: The liquidity problem is something else again.

MRS. GILLELAND: We have covered that. You know what we think about the liquid assets, it is on page 6, the lack of them. I don't see how a middle-sized estate, somewhere between $60,000 and $75,000, can make any suitable provision of liquid assets. Our argument is certainly set forth there. That is exactly what we think.

" If the husband dies early, liquid assets will not be needed to pay estate tax because the estate will not have reached a taxable aggregate; if he lives to middle

" life, a growing business requires all available capital to keep it growing into a taxable estate (or, as the married couple think of it, one that will keep them through their retirement years). For many years the first call on liquid assets must be provision for the education of the children. His pension, if he has one, will provide a basic subsistence allowance for the couple, and later for the widow; --"

That is the way they think of it. They don't visualize the capitalization program. They think about that pension in terms of a basic security. Now we have had not just scores but hundreds of women, widows who have told us of the surprises that came to them in the capitalization of the pension which made their estate taxable and the fact that not only do you have to pay it in six months' time -- there is the horror story you told me yesterday afternoon, Mrs. Bishop. Mrs. Bishop is a widow and went through this. You have to pay it in six months but maybe it is not settled in six months. You have to pay the interest and pay to get the provincial assessment of $20,000. Will you tell us the story about this, Mrs. Bishop?

COMMISSIONER PERRY: Perhaps we could spare Mrs. Bishop the story.

MRS. BISHOP: As a matter of fact the reason I am on the committee is I went through it all and I felt that anything I could do in any way to

alleviate this situation and keep other people from having to go through it I will be very glad to do. It was entirely a surprise to me. My husband thought he was leaving everything in very good shape for me. My estate was just small. He didn't take into consideration at the time, he had been ill, the capitalization of the pension. When it came up I must say the Dominion Government were very fair. We had to act under the law.

They had an assessor come and assess the estate, which they do, which I paid for. You pay for the assessor to do the work. My son is a chartered accountant and he had all the assets and everything in detail and he handed them to the lawyer. The lawyer said they would get in touch with the Provincial Government.

The Provincial Government said, "We will send an assessor". We said, "The Dominion Government has accepted the assessment. It is here in Ottawa". They said, "No, it will not do. We will have to send our own assessor". After four months they sent their assessor down with the tape measure and he measured everything fore and aft and went to Toronto and raised the estate by $20,000.

Then I spoke to my lawyer and he said, "We will just protest that." I said, "I don't know about protesting, that costs money". As you know, legal fees in connection with it are not small. So my son went to Toronto and when he went to see the man in Toronto the man said, "It may be a little bit

high. We always like to err on the right side. We sort of expect these protests to come in."

That seemed to me the very last thing to have an official who is supposed to be efficient come down and create a situation in which it was going to cost more money. You get so worried having to pay for this and that. They did reduce it some but not altogether, about $10,000. Eventually we got everything ready to be paid and was paid and in six months all the succession duties and everything were clear.

What I feel very keenly about is that there is an awful lot of administration that might be simplified.

THE CHAIRMAN: I don't understand what the payment was you made in respect of the assessor. Was it travelling expenses?

MRS. BISHOP: Yes. When they ask to have the estate assessed you engage an assessor to assess your estate. In this case it was in Ottawa, Mr. Ross, who is dead now. He makes a charge to you for assessing the estate and you pay it.

THE CHAIRMAN: This is evaluating the property?

MRS. BISHOP: Yes, the realty.

COMMISSIONER GRANT: Was that what is sometimes called an appraiser's fee as distinct from an assessor's fee?

MRS. BISHOP: Yes, I think that is the appraiser's fee.

COMMISSIONER GRANT: That is an Estate matter, not anything arising out of the Succession Duty Act or the Estate Tax Act. The Government provides assessors but at no charge to the estate.

MRS. BISHOP: The Government assessor does not put any charge on the estate.

COMMISSIONER PERRY: The appraiser is not an official.

MRS. BISHOP; No. Your Ontario assessor is a Government official.

COMMISSIONER PERRY: Is this the man you paid?

MRS. BISHOP: No, the man I paid is the man in Ottawa.

COMMISSIONER PERRY: A man in the business of making appraisals?

MRS. GILLELAND: Yes, but you have to pay that.

MRS. BISHOP: The lawyer suggested that this was the procedure. I don't know why.

THE CHAIRMAN: You did fairly well to get the estate settled in six months.

MRS. BISHOP: Yes, ordinarily it goes on and you have to pay added expenses in getting it fixed up. It just happened that we had some money we intended to do something else with but it was not there to do it with after the Succession Duties were paid.

MRS. GILLELAND: We really don't have to take this brief point by point. We are covering

the points relating one to another.

THE CHAIRMAN: I think that is the best way to do it. I am quite happy. You were about to change the subject and we moved on to page 6.

MRS. GILLELAND: Before I get to page 6 I would like to go back to page 5.

THE CHAIRMAN: You lead us, Mrs. Gilleland.

MRS. GILLELAND: This point on page 5 in paragraph 11 is headed, Delay in Collection with Estate Taxes. We are asking that there should be no collection of estate taxes on a married couple's estate or estates -- I don't know whether to use the singular or plural there -- until both spouses are dead. Now hundreds of times literally -- this is not a rough figure at all -- hundreds of times we have had this argument about the Government has no right to tax that estate until the wife is through with it or vice versa.

I know it is a brand new idea -- I guess I won't finish that sentence. We have had it submitted to us by widows who, of course, cannot benefit it by future changes in the law. They are the people who have brought it to our attention.

I don't think of it. My husband is still earning and as long as this is going on you are never going to think about this at all. You just think it is always going on the same way until your friends -- and you get into a Committee like this and people come to you and tell you what has happened.

Now I am literally saying that hundreds of

widows have come to one or other of this small executive group and made this statement. You know, the very first time I heard it I thought, "Oh, yes, that would be nice. Maybe there is something in it". That is as far as the idea got with me because it seemed too remote kind of thinking. When I have had it hammered at me over and over, this resentment, we begin to see this is a pretty reasonable thing and in this case we are moving to the philosophical approach, I don't know any better word than that, of what constitutes proper and reasonable kind of taxation. Now here is capital removed without benefit. Now I know there are implications in implementing this.

COMMISSIONER WALLS: There is one thing that quite puzzles me. I can understand the sentiment behind it but what about if they remarry? When does the estate stop?

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I even worked out an extreme example where it would never stop. In other words, if a man age thirty is married and at age seventy his wife died or is divorced from him, he remarried a woman of thirty and lived another five years and died, and she married a husband the same age as herself and then he lived to seventy and went through the same process either divorcing his wife or his wife dying, this could go on ad infinitum and the estate would never be settled.

The thing that bothers me, and I know that is an extreme case, but it would be possible literally for an estate never to be settled. What is the answer to that one?

MRS. BISHOP: The answer to that one is there are hundreds of thousands of widows in the other category against your special case that you build up, and why penalize the hundreds of thousands for the sake of one? Any law should benefit the greater number. I grant you that there are specific cases, but ordinarily the husband and wife have worked together, they have earned or cared for what they have in order that they may have something in their declining years. If a wife dies first and the estate belongs to them both, if there is a pension it comes in; they have their home and the husband is able to continue like he did before without any change whatsoever.

However, if the husband dies first his wife is immediately confronted with (1) succession dues,

and (2) half the pension, and these have to be settled right away, and if there are not any liquid assets -- and it is at a time when she is really grieved and has no protection and ordinarily it is in her later years. She has to reduce her way of life; she has to confront all these legal aspects of settling up of the estate, and why not make it that the government doesn't take any taxes out of the estate until such time as they are both through with it?

COMMISSIONER WALLS: Would you give consideration to the fact that the government required settlement of the estate if the survivor remarried? That might be the solution to this. If the survivor remarried the government steps in?

MRS. BISHOP: I think there could be some clause put in that could perhaps care for that situation, but why penalize, as I said before, the hundreds of thousands of people who really suffer? I know dozens and dozens of my own personal friends, widows who have gone through this over and over and over again, and it is not funny. It really is not.

I do think it is unfair to have the two situations of handling it; the widow who is really perhaps not capable unless she has some help of going through this, just because she is a woman that she should be penalized whereas on the other hand if her husband survives he is able to carry on his way of life.

Sometimes people who have a home and

half a pension are unable to live in that home because they have not enough income to carry on and live in it. The Government says right away you have to pay your succession dues, and if they did, they would not have bread and butter -- if they wanted to live in their home they would not have bread and butter for about two years.

MRS. GILLELAND: We know of a specific case where this was so, and it was a deputy minister's wife.

THE CHAIRMAN: Would you not think in most cases the husband would leave the use of the estate to his wife? Of course I suppose what you propose would accomplish that result without having to conform to that part of the law which he may not understand.

MRS. BISHOP: You mean when the use of the estate is left to the wife there is no succession dues?

THE CHAIRMAN: It is placed in trust with the estate passing down to his heirs in the next generation.

MRS. BISHOP: Yes.

MRS. FLAHERTY: We do not presume to tell the husband how he should leave his estate. Many husbands feel that the wife has made a contribution and she is the one who should benefit from the estate that they have built up over the years. The children

are out earning their own money and the wife has the first claim.

THE CHAIRMAN: It is an interesting thought indeed.

MRS. FLAHERTY: And to answer Mr. Wall's extreme case, all the time this marriage and divorce and remarriage was taking place, money is being spent in the country; income tax is being paid and sales tax is being paid. There is revenue from that money although it may not be in the specific category of estate tax, yet the revenue from that money is not completely lost to the government.

The revenue, as I have pointed out, from the estate tax is so small in the revenue picture that the loss of that specific amount that you are discussing would not show anywhere.

MRS. BISHOP: Another thing I would like to say is ordinarily it is not such a long time between the time -- perhaps it may be some years --- before the government would collect the succession dues, we will say, when the wife dies, and that if they feel they should have the succession dues then, why not raise the rate, and when they do get it, it would easily make up for it, and it would pass on, because the people who would inherit it, perhaps they have had no part in either earning or caring for it.

I have two sons which agree with me entirely on this. That is all I can say. They feel

this very keenly, that the father and mother who have had this should both have the use of it until they are both through with it, and then if the Government wants to collect the succession dues or duties, raise the rate of the tax which would equal it off.

COMMISSIONER GRANT: To put this proposal that you are now urging in its proper perspective, would you agree that your reason for wishing to defer the tax on one-half of the estate until the death of the surviving spouse is that the tax which would be paid to the Government at the time of the death of the husband, let us say --

MRS. BISHOP: Yes, that is what we are dealing with.

COMMISSIONER GRANT: That money would be retained in the estate and be available to the widow either by way of income or by way of principal or both? Am I correct?

MRS. BISHOP: You mean that the estate should not change? She would really not have access to the principal?

COMMISSIONER GRANT: No, no. What I am saying is this: In urging that one-half of the estate be the property of the surviving spouse and not taxed until the death of that spouse, your reason for that is to conserve in the estate the amount of the tax that would be paid if it were paid at the death of the first spouse?

MRS. BISHOP: Yes, I think so because after all I do not think it belongs to the Government until such time as they are both through with it.

COMMISSIONER GRANT: In urging that one- half of the estate should be regarded as being owned by the surviving spouse and not taxed, then the only advantage -- and I do not minimize it -- but the only advantage to the estate is that you are getting the use during the lifetime of the surviving spouse of the money that would have been paid in tax?

MRS. BISHOP: Yes.

COMMISSIONER GRANT: Therefore, do you differentiate between the size of estates? For instance, if a person left a one million dollar estate, would you say that on five hundred thousand of that, the tax should be deferred until the death of the surviving spouse?

MRS. BISHOP: I think what should apply to one should apply to the other regardless of the size of the estate.

COMMISSIONER GRANT: Or do you differentiate as to the need? You do not differentiate?

MRS. BISHOP: Well, no, I really believe in the principle of it. I think the principle is that what the husband has the country does not claim until he dies, and that in a true marriage the country should not claim the money until the wife is dead because I do not think it belongs to the Government until such

time as they are both through with it. You are immediately making a difference between the husband and the wife, between a man and a woman, let us say that.

COMMISSIONER GRANT: Let me explore it a little further.

MRS. BISHOP: Yes, I am glad to have you do it.

COMMISSIONER GRANT: I note this is a very important part of your brief, and I think you lay great emphasis upon it.

MRS. BISHOP: I do personally because I have experienced it. I find, just as Mrs. Gilleland says, until you experience these things you are not aware of them, and letters we have had from all across Canada about the hardships that widows have gone through all across Canada in settling the estate and what they have had to give up.

I can speak especially about the farm women on farms in the west. They were just coming in hundreds from the people there; what they have gone through. They never even thought about it, but it does not take much of a farm and all the machinery and animals to build up over $50,000.

Now, in order to pay that tax sometimes they have had to sell -- they have written in and said that they had to sell machinery that produced their income in order to pay their Government taxes. Animals

had to be sold. The estate has to go down. And here she is in her declining years. I mean with the financial set-up --- emotionally what she goes through is most pathetic.

COMMISSIONER GRANT: You are urging that the exemption be raised. You are also urging that one-half of the value of the estate be regarded for taxation purposes as owned by the surviving spouse. If the exemption were raised to, say, $100,000, would you feel that you would press this second point to the same extent?

MRS. BISHOP: I think that a person who has been used to living on, let us say, $100,000, is just as much entitled to go on living as she has been living up to that time. If they have to reduce her living to just a substance just because that is there --- I think the principle applies just the same.

COMMISSIONER GRANT: Do you think there should be any security taken for this deferred tax?

MRS. GILLELAND: In leaving the money in escrow, is that the idea?

COMMISSIONER GRANT: Say that the tax on one-half of the value of the estate was estimated to be $5,000 at the death of one spouse, do you think there should be any security? The assets might become dissipated entirely by the time of the death of the surviving spouse.

MRS. GILLELAND: Do you mean this $5,000 tax would be reserved? A reserve fund but that the widow would have four and a half or five per cent or five and a half per cent or whatever the going rate of money is as part of her income?

COMMISSIONER GRANT: The tax would not be taken out of the estate.

MRS. GILLELAND: It is for her use.

COMMISSIONER GRANT: But there would be some principal --

MRS. BISHOP: Yes, I think that would be quite fair. That would be quite fair. Whatever the hardship is in most of the correspondence, the great hardship is making up that payment of succession dues at a time when there is not that asset there to do it. It has to be taken out of something that she should have the income from until she is through with it.

COMMISSIONER GRANT: I would venture to state that many people in planning their estates take care of that situation.

MRS. BISHOP: They do that with insurance. In insurance in some cases, or at least in a great many cases they do, and I do think that men do provide that way. Of course they have had to pay for it during their lifetime, but that is one of the things they do.

However, when I say that a great many people do not realize it, I do think that people are very much more conscious now of what succession dues

mean than they have been in the past.

COMMISSIONER GRANT: Then you are aware no doubt of the provisions of the Income Tax Act which will permit under the gift tax provision of the Income Tax Act --

MRS. BISHOP: $10,000 can be given without any taxes during the life, yes, I am aware of that.

MRS. GILLELAND: Once.

MRS. BISHOP: Yes.

COMMISSIONER GRANT: And that applies to farmers as well as others.

MRS. BISHOP: Yes, but I am speaking now of the Exhibition where farmers come in and ask again and again and again for these blue sheets, and they were astounded. They couldn't understand that this was really the law, and they went home with a very inquiring mind into the situation, and heartily agreed that it should be a joint partnership.

MRS. GILLELAND: May I say, Messrs. Commissioners, that whatever safeguards would be appropriate for the collection of the necessary amount of tax -- I will go back -- that the necessary safeguards for that established by regulation in amendments or drafts, that is fine, providing the principles that we are after in relation to the recognition of the wife's contribution to the total estate, in so far as that is implemented, then we are going to be more than satisfied women because at the moment we consider that on

the death of the husband the widow becomes a sort of second-class citizen.

Things are taken from her that we think the Government has no right to take. These are things that she has helped to acquire. This is the basis of this. Now, take all the safeguards that are necessary to get the tax paid eventually, but it should not be so -- I don't care if it is $1000 of tax -- it makes no difference to the principle or whether it is $5000 or $10,000 that is taken.

THE CHAIRMAN: There is one point I do not quite understand; when is the amount of an estate determined? Do you mean it would be determined upon the death of the first spouse or on the death of the second spouse? You have suggested that whatever is left is for the benefit of both partners to the marriage, and if that is the case, should the surviving partner who is entitled to the asset in that estate be at liberty to spend the entire estate or should the surviving partner --

MRS. GILLELAND: From the standpoint of what is right morally, as far as we are concerned, practically speaking I do not care if she goes to Hawaii. I don't care if she puts it down the drain; it is hers. She has helped to gather it. That is a foolish thing I have said, and she is not going to do it. It wouldn't make sense. After all, women are sensible people too, by and large, But from a

practical point of view I will answer you in a very different way and say that I can see very well that the preservation of half of the estate in order to make sure a taxable specific amount -- her half is her half and I am going to spend mine as I like or save it. I am a saving kind of person so I am going to save it.

THE CHAIRMAN: I understand your point.

MRS. GILLELAND: Does this make it that this is a reasonable thing from a taxation point of view to have a sum established at the time of the death of the husband and base taxation on that but don't remove the money from the estate so that the capital will not be removed from the estate and it will be available for the use of the wife.

COMMISSIONER GRANT: You are assuming, I believe, that if for taxation purposes the wife would be regarded as the owner of one-half of the estate, you are assuming that that is in accordance with the husband's wishes although it may not be.

Have you given consideration to this in the stand which you are taking: Should the husband provide the widow he leaves with something less than she would get if she owned one-half of the estate?

MRS. GILLELAND: Yes, we have, and we still know very well that it is every person's right to make their will as they wish, and if there are a few ornery husbands who do not want to leave their wife

a penny, then the widows will take recourse to the law, for what it is worth, and so on.

However, as for setting up legislation within the Estate Tax Act that would prevent a man or women from making a will in the way they like, I do not think there is anything sensible about that. We are not asking that. You must preserve the individual right of a man or woman to make a will any way he or she sees fit.

COMMISSIONER GRANT: I am glad to hear you say that because to rule otherwise by statute would be violating one of the most basic principles.

MRS. GILLELAND: Yes, and violating what is right, a civil right; you would be denying a civil right.

COMMISSIONER GRANT: And in the establishment of a trust, it must be honoured, and it must be maintained provided it is within the law.

MRS. FLAHERTY: In our submission at the bottom of page 2 we say:

> "We submit that one--half of a deceased marriage partner's estate should, if it passes to the surviving partner, be considered for tax purposes, as earned by the surviving partner, and not therefore subject to estate taxation."

COMMISSIONER GRANT: If it passes.

MRS. FLAHERTY: Yes, if it passes.

MRS. GILLELAND: That is the key phrase.

COMMISSIONER GRANT: Now, the estate does not pass if you base it on a life interest.

MRS. BISHOP: No, that is right.

COMMISSIONER GRANT: And today I suggest that the vast majority of wills restrict the gift to life interest with the right to withdraw on principal.

MRS. BISHOP: Yes, I think so too.

COMMISSIONER GRANT: In that case your submission would not apply?

MRS. GILLELAND: No. We only ask that it apply in cases where it can apply, and in time if lawyers make husbands' and wives' wills differently, more will benefit by the new legislation that embodies the principle we are asking for. If it only benefits less than half now, the principle is established, and then the course of how wills are made will take their course.

MRS. THOM: The main reason for having a life interest is, I think, to get around the Estate Tax Act. If this is removed, that won't happen so often; if there is a method of passing half the estate to the wife.

COMMISSIONER GRANT: It certainly is a factor in having a will drawn that way. Whether it is the main factor or not is another question. The main factor might be that the husband says, "Well, I do not think I want to give my estate outright to

my wife," regardless of tax considerations.

MRS. THOM: I do not think that is the modern view of the younger generation, for I can speak for that, and I feel a lot of them speak of the co-operative movement, and I know when I was working we didn't think of it as my money or my husband's money. We thought of it as our money, and we did not arrange our estate or the small estate we have at the moment in terms of his and hers. It is all ours. But that would hurt me more than it would hurt him if he died.

MRS. BISHOP: I haven't anything to say as far as a will is concerned. My husband left everything to me outright without any tags to it at all. I mean I haven't a grudge, don't think, or anything like that. But even with the simplest way of distribution, which could not be any simpler, there were still all these complications that came up. I do not think I was more sensitive about it than the great majority of women have been who have gone through it. For that first year when you are going through a very trying time.

COMMISSIONER PERRY: I was wondering if I might ask one more question. I am frankly confused by what I regard as your second and third proposals; one being only half of the estate passing on the death of the husband and the other being none of it passing on the death of the husband. Is there any distinction between the circumstances which they

would apply to?

MRS. GILLELAND: No.

COMMISSIONER PERRY: Or is one of those better than the other?

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MRS. GILLELAND: I will put it this way: Our last point is an advanced philosophy. Let us put it that way.

COMMISSIONER PERRY: May I tell you in fact it is not?

MRS. GILLELAND: For us it is.

COMMISSIONER PERRY: The original concept was it should be a tax on passage of property between generations. In England, for example, it was the duty that the Crown levied on passage of an estate from the father to the oldest son. The thing that is new is the tax on passage of property between people in the same generation. Historically you are on pretty firm ground whether this will help you or not.

MRS. GILLELAND: We are glad to know that historically we are sound. As far as we are concerned the proposals to which you have just referred would solve everything that went before. As far as married women we are still under the $75,000 ~~true~~ exemption. To use the short identification words, "half" and "delete" then in a way they are related for the simple reason if that half is established the tax -- I don't think you can get No. 3 to delete without some action for point 2. If half the estate is regarded as belonging to the wife the tax is set on the husband's estate assuming he dies first and then valuation of tax can be set at that point and it would be half the estate, so in a way there is a relation between 2 and 3.

COMMISSIONER PERRY: The husband's half would be evaluated?

MRS. GILLELAND: Yes. I don't think we can present 3 without presenting 2.

COMMISSIONER PERRY: I would disagree. I would present 3 on its own merits.

MRS. GILLELAND: We don't mind doing it that way. We don't mind at all.

COMMISSIONER WALLS: Other people call it the thin edge of the wedge!

MRS. GILLELAND: This Estate Tax Act, as it now stands, at the moment of the husband's death when he predeceases his wife it demotes the widow economically and psychologically and a set of measurements for the value of the wife are used in calculating that estate that never in the life of the husband had been used by him in his evaluation of his wife nor in reverse, her of him, nor their opinions of what is his and hers and ours, nor in the family. The wife and mother has had a status during the life of her husband that she loses the minute an estate begins to be administered. This is the principle that we object to and object to emotionally certainly but also we have good solid grounds outside of the emotional.

THE CHAIRMAN: Thank you very much. You have given us a great deal to think of. This has been most interesting and stimulating and we will continue to think about it, I assure you.

MRS. GILLELAND: Thank you very much.

MRS. THOM: That is all we can ask.

---A short recess.

THE CHAIRMAN: Are we ready?

THE ADMINISTRATIVE OFFICER: Mr. Chairman, on February 18, 1963 the Commission received a brief from the Canadian Federation of University Women. The Federation is represented here this morning by Mrs. M.J. Sabia, Vice-President, Central Canada. Mrs. Sabia will introduce her associates and speak to the brief, which I would like to enter as Exhibit No. 87.

---EXHIBIT NO. 87: Brief of the Canadian Federation of University Women

SUBMISSION OF THE
CANADIAN FEDERATION OF UNIVERSITY
WOMEN

APPEARANCES:

Mrs. M.J. Sabia,	St. Catharines.
Mrs. S. Tench,	Ottawa
Mrs. W.R. McClelland,	Ottawa.
Mrs. R. Orange,	Sudbury.
Mrs. Frank Flaherty,	Ottawa.

THE CHAIRMAN: Thank you. Good day, Mrs. Sabia. Before getting into your brief would you be so kind as to introduce your associates? We would also like to know more about your Federation. I note here that you have 107 member organizations. I was not very clear what a member organization is. Would you tell us more about it?

MRS. SABIA: Thank you, Mr.Chairman. We appreciate the privilege of coming to the Royal Commission to present this brief to you.

Our Federation, as is stated here in this brief, has 107 clubs throughout Canada. There are clubs from Atlantic to Pacific, the greatest number being in the Province of Ontario, some 60 clubs, and the remainder in the rest of Canada.

We represent somewhere over 10,000 graduates of universities who are extremely interested in public affairs, education, and various facets of our economic life.

Now there is not any doubt that when talking of taxation that it is rather difficult to be too certain, to be too emphatic about anything. Taxation is a vast problem. It is a powerful instrument in the hands of Government to control and manipulate our Canadian economy. There are not fast rules and we don't pretend to have any fast, clear, and concise recommendations. These are flexible ones. They are recommendations that we have talked about in our clubs, that we have considered and that we have studied. They are not the answer nor the end to taxation.

In the past few years there has been a growing awareness, I think, among women, among men, among all Canadian citizens of the rather crippling and confiscatory level of taxation in Canada and the damage it does have to our Canadian economy in this vast country of tremendous expanse and very few people.

In looking at this we realize it applies to all levels of taxation and not only the ones we ourselves are interested in. We are interested in the level of taxation that hampers the ability of Canadians to invest in their own economy and country because of personal income tax and estate taxes.

Now we have limited ourselves today to a few specific facts. As I said before they might not be the answer. We realize the Royal Commission was set up to look into all facets of taxation. Perhaps a whole new thinking, a broad new thinking should be looked at rather than a specific type of change or amendments to amendments. We have had so many amendments to amendments, which has increased the horrendous taxation that we have, crippling as it may be.

Now I am just going to give you specifically the three points of personal income tax and the three points of estate tax rather briefly and I shall ask the women on the panel to speak to them.

On my left I have Mrs. Orange from Sudbury. On my right there is Mrs. Tench of Ottawa and next to her Mrs. McClelland of Ottawa and next to her, you have already met Mrs. Flaherty of Ottawa. All of us have worked on this brief on taxation.

We have three points in personal income tax. First, the wife who is only allowed to earn $250 before exemption is taken off her husband's allowance for her. We would wish or feel that she should be allowed at least $950 that the child is

allowed, or the son or daughter or other dependent is allowed to earn. This is certainly just asking for a certain amount of equity, be that as it may.

Secondly, in personal income tax we would mention the discrimination against the employed spouse. That is the woman who is working either for her husband in a small business, for a professional man, a small salesman, or this kind of person who works with her husband and is not allowed to take that as a legitimate expense. This is something that is discriminatory against women and we feel something should be done about it.

Now the third thing on the personal income tax is that a deduction be allowed for salary paid to a housekeeper when both people in the home are working or when one is working and there is someone else in the home. We feel this is a legitimate expense. More and more women are moving into the labour force today. Twenty per cent of the married women are working and we feel that some relief certainly should be given to them if they must employ someone to look after the children or other dependents, be they old parents or sick brothers or sisters. These are the three in the personal income tax bracket.

Now in the Estate Tax we also have three. Sometimes we have wondered about this, I must admit, but nevertheless we have worked on it and talked about it and that is the true exemption of $50,000 on all estates rather than the $40,000 granted today. All estates are allowed $40,000 and $60,000 where there is

a widow. We are asking that all estates be exempted $50,000. We are also asking, again this is a contentious issue, we would prefer to have a true exemption of $100,000 and not worry about the equity in the marriage partnership. We bring it forward because it is discriminatory against women. We do feel there ought to be some kind of equity in recognition of the marriage partnership. Again I think we would prefer exemption, if this is possible. We realize this could be manipulated in many ways and we give it to you as our feeling, as our study.

The third is the exemption of pension benefits from estate taxation. This is a very important item because you know men today are providing superannuation or providing pensions, Government annuities, whatever they may be, for a wife and then suddenly she finds it is taxed on her life expectancy. This is again discriminatory. We feel that money that has not actually been received should not be taxed and this we lay great emphasis upon.

To start the ball rolling I would like to ask Mrs. Tench to speak about the discrimination against wives as dependents. Would you briefly state the facts?

MRS. TENCH: I think Mrs. Sabia has made it clear already what the discrimination is. On the income tax form it is quite clear that any

dependent, son, daughter, father, mother or any dependent claimed by a taxpayer can earn $950 a year before the taxpayer is not allowed to claim them as a dependent. In the case of a wife she is only allowed to earn $250 and after that his tax exemption is affected. It is reduced over and above the $250. We believe that this is not fair and is a discrimination against wives as against any other dependent.

THE CHAIRMAN: Thank you. Perhaps one way to cure that might be to reduce it in the other direction.

MRS. TENCH: The trend in the past number of years has been to up the amount of money allowed, that a dependent is allowed to earn before the exemption is cut off or decreased.

THE CHAIRMAN: Thank you. Before we move on to the next point could I inquire if there are any questions?

COMMISSIONER GRANT: I was wondering if you would make any distinction between investment income and earned income on the part of the wife?

MRS. TENCH: No, I would not.

MRS. FLAHERTY: No distinction is made among other dependents. Why should it be? A father could have earned income and earn up to $950 before the taxpayer's exemption is reduced.

MRS. TENCH: A parent could receive the

old age pension in addition to another pension, which is not earned income.

COMMISSIONER GRANT: I think there is a distinction in this respect. If the wife has earned income then she must be spending some time out of the home to bring that money in and therefore the husband is deprived of her services to that extent. Your argument might have more force with respect to earned income than it would with respect to investment income where she is under no handicap as far as household duties are concerned.

MRS. TENCH: I don't think today husbands look on wives going out to work as an encroachment against their duties.

COMMISSIONER GRANT: Shall we say that might be a matter of opinion!

MRS.SABIA: I think the greater increase of women in the labour force is a fact of life. There is not any doubt about it. We cannot further deprive ourselves of the brain power of half the population. You have women who are educated, who have great skills, lawyers, doctors, trained accountants, even if they are stenographers in an office they are needed and I think that 50 per cent of the population ought to be treated as the other 50 per cent.

I think with the labour-saving devices today that the woman who leaves her home does not always deprive her children or her husband of the

services that she should render in the home. We are all aware of the fact that women are going out more and more, whether we like it or not. We have to readjust our thinking and our taxation thinking on those levels.

MRS. TENCH: The $950 that a married woman could earn does not prevent her from keeping up with her duties very much because that does not take much time to earn $950. This is a part-time job.

COMMISSIONER WALLS: You don't recognize the initial $1,000 deduction for a wife, which means a total exemption for a wife of $1,250.

MRS.TENCH: If it were a dependent --

COMMISSIONER WALLS: A dependent would get $950 plus $350, which would be approximately the same amount as the $1,000 married exemption plus the wife's $250 allowance.

MRS. TENCH: If a man is a widower and has a child he can claim $1,000 for that child and the child can earn $950 and the wife cannot.

MRS. SABIA: There is tinge of discrimination.

COMMISSIONER PERRY: May I say a word on behalf of the unmarried woman? It could be said that the situation here would be that the exemption for two people working would be three times the exemption for a single unmarried person working. I think one would have to define this proposition

that the State is so anxious to have married women working that a much greater exemption would be given than to where an unmarried single woman was working.

MRS. TENCH: If a man is single and has no responsibilities he gets $1,000 exemption the same as a single woman. If a single woman is supporting a mother or father she gets an additional $1,000 exemption and that parent can earn $950 a year either by investment income or earned income.

COMMISSIONER PERRY: I appreciate the point of the dependents. Let us leave dependents out of this and speak of the married couple as opposed to a single person, be it male or female. Your suggestion in effect is that the married couple be given a total exemption of $3,000?

MRS.TENCH: No, $2,000.

COMMISSIONER PERRY: Would not the husband be allowed --

MRS. TENCH: If you have in mind that any other dependent that he has --

COMMISSIONER PERRY: I have deliberately left dependents out of the argument.

MRS. TENCH: That is what we claim is inequal. For any other dependent he has he can claim $1,000 for the dependent and that dependent can earn $950 a year so he gets $2,950 exemption, if you look at it in that way.

COMMISSIONER PERRY: Suppose I make the

great mistake of conceding your argument. Let us say for the record that I am and this is a horrible inequity. Let us get back to my case where you have a wife and husband working and where the husband would be allowed exemption until his wife's income exceeded $950. Would not the total exemption be $2,950?

MRS. TENCH: Yes, which would be the same exemption for any other dependent that he had.

COMMISSIONER PERRY: We have stopped that argument. We have agreed with you. Now opposite that wife or husband is a single man or woman whose exemption is $1,000. He, in effect, is being given $500 less exemption than either one of the other parties. I am not putting this as an artificial case because I was in the Department for years and years and this was the sort of correspondence that we got from single women. Why bless further our already blessed sisters!

MRS. SABIA: If blessed they be! I am quite sure that our whole Federation to a man, or a woman, would very whole-heartedly agree that the single woman should certainly be given as many concessions as the married woman. We make no distinction between them. It is the married woman's case we have stated here because it shows up so badly. It is the married woman in part-time work in the labour force. We are not jeopardizing the

single woman. We feel she should have equal exemptions. I think the single woman today is not on a parity with the married woman maybe because the married woman is so vocal about things she is not getting. The single woman of today is a very productive part of our economy and should certainly be granted every advantage and every exemption of the married woman. I am sure our Federation would go along with that.

COMMISSIONER PERRY: We may give you an argument in your own favour. It is expected of a married man in law that he support his spouse, which is a rather vague term. One would think if he gave her a little bit of money occasionally he was supporting her. The law requires that a child be wholly dependent, not have a cent of its own, yet this is the area on which they are allowed to earn $950.

THE CHAIRMAN: Are there any other questions? I think you have taken care of it, Mr. Commissioner.

COMMISSIONER PERRY: We have conceded that argument.

MRS. SABIA: Compromise, you know, is the value of these things.

MRS. TENCH: But there is a discrimination.

MRS. SABIA: Let us not belabour it.

COMMISSIONER PERRY: I think we get the point all right.

THE CHAIRMAN: The next item is paragraph 7.

MRS. TENCH: I believe that in the past the Income Tax Act allowed wives to work for husbands and this was changed and now wives are not allowed to work for husbands and the husbands to claim the wages paid to the wife when she is performing services the same as would be performed by an outsider. We believe the husband should be allowed to claim this as a business expense and the wives should be allowed to declare the income earned as a separate income.

THE CHAIRMAN: You are not alone of that opinion. We have heard it two or three times and of course it is a fair and fundamental point, I think. There is one question that I would like to ask you about because I have wondered about it for a long time. It is the belief that taxation be levied on the husband and wife jointly rather than the individuals.

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I might say that I have had my own views on it. I do not want to commit myself on it, but I have been intrigued with the idea. Have you ever considered the possibility of recommending a joint return for husband and wife in line with the American system or the system in certain European countries? There are a number of different ways of doing it.

MRS. SABIA: Yes, I think we have.

MRS. FLAHERTY: We have discussed it.

MRS. SABIA: We have looked into the American system. They can elect to either make their tax return jointly or else separately.

As I say, our recommendations are flexible. We have gone along the thinking of the Bar Association and the Canadian Institute of Chartered Accountants who have felt this very strongly, and they are experts in their field. We have studied what they have recommended, and we have felt it was a good thing. We would be very much in favour of the American plan. We have gone into it and we felt it was a good thing.

Our idea in presenting it this way is the fact that we always believe if someone in the community or in the country has done an intensive study and it is a good study, let us pick those brains, let us use that and let us go from there, and that is I think what we have done in this recommendation.

THE CHAIRMAN: I raise that only to find out whether or not you are against it, and it was not in your submission.

MRS. SABIA: No, we would not be against it.

MRS. FLAHERTY: All these presentations that we are making have been the subject of study over a period of years, and although we have discussed the possibility, we are not prepared at this moment to bring it up as an argument.

THE CHAIRMAN: That is fair, I would think.

MRS. SABIA: Are we going now to the next point?

THE CHAIRMAN: Have we any questions on this?

COMMISSIONER MILNE: I do have a question. It is difficult to get statistics on this. We have statistics on the number of women who work and we have statistics on many things, but it is difficult to find out how many women work for their husbands and also to classify even further into the fields of activity.

It certainly would seem in the professional field, certainly the earnings of the wife as a business expense are probably not as important because of the factor of costing the service performed which is recoverable in the business in the professional

fee. However, I am thinking about other areas, and I wondered in your research if you have anything that would be conclusive that you could give to us?

MRS. TENCH: I think that if you look at any corner grocery store, for example, you will find that the wife is working.

MRS. SABIA: I do not think we specifically have statistics. We do not have.

MRS. TENCH: They are not available.

MRS. SABIA: I think you are quite right in saying on the professional level it is not quite as important. I think your small business man -- I think back in my own home town of the women who work in these dry cleaning establishments with their husbands, and they haven't the money to go into a limited company or anything like this, and they are uneducated women but who know and feel they should be paid for the services they are rendering into the business and yet it is not a deductible item on their husbands' expense.

We haven't even taken a look into the statistics of this. I do feel that the small business men more so than on the professional level are the people who have been discriminated against because many a woman has helped her husband in this field. I am always reminded about the little joke about the multimillionaire and someone asked him what he attributed his great wealth to and he said it was my good wife who

wanted to see what income she could live beyond.

Here is a woman who worked hard and tries very hard even though she spends the income and she is not allowed anything for it. He is not allowed to deduct anything. I think this is the greatest discrimination. I feel quite sure, Mrs. Milne, this is more so than on the professional level, and even though professionals have a point, I would rather concede to the small business man.

MRS. FLAHERTY: There is no area that statistics could be made available. For one thing a man can't report his wife as working for him. There is no place for him to put that down. In the census figures the wife can sign herself as an unpaid family worker, and in the labour force survey that is taken every month there is a place for an unpaid family worker. If we were able to get access to the results of those punch cards, we would find it. The wife in turn who is working in keeping her husband's books if he is a doctor, or if she is working in the store, she can't declare income so there is no place for her to go on record that she has been helping so the statistics would be very hard to come by.

THE CHAIRMAN: I certainly understand the injustice of not permitting a deduction in these circumstances. However, I do concern myself a little bit about the man with the corner grocery store who employs a clerk to work in the store and the wife looks

after the child and the house and the kitchen and is not paid for it, whereas if you put it around the other way he would get a deduction, would he not?

MRS. SABIA: I have great faith in the Department of Internal Revenue in finding out these things. They have a way of looking into things and knowing what is going on, and I think quite legitimately so, that there has to be some way of making sure, you know, that you are not dealing at arm's length, so to speak. Certainly there are ways of finding that out and making sure that advantage is not being taken.

MRS. TENCH: The possibility of evasion exists for the higher income groups and non-professionals because they can form limited companies and pay wives' salaries whether the wives are working or not.

THE CHAIRMAN: I was not thinking of evasion particularly. I was thinking of the difference between the wife working in the store and working in the kitchen. In the store the husband gets a deduction, and in the kitchen he would not. Is that quite fair to the wife working in the kitchen?

MRS. TENCH: Often the wife combines both. She works in the store and in the kitchen and has a child under her feet.

THE CHAIRMAN: She should get a right good deduction.

MRS. SABIA: She should get a good deduction there.

THE CHAIRMAN: Are there any more questions?

MRS. SABIA: I think our next point is on the housekeeper's wages. This again is a bit of a contentious matter, but we feel a little strongly about it and I am going to ask Mrs.Orange to bring it forward.

MRS. ORANGE: I do not know that I can add to what Mrs. Sabia has already said and what we have included in the brief, but we do accept the fact that there is a new look in women in industry and in the professions, and married women are being encouraged to go back and take their place in the labour force.

MRS. SABIA: Single women as well.

MRS. ORANGE: And if there are dependents that must be cared for at home, we feel that $1,000 exemption should be allowed for the salaried person who is employed in the house to look after the child or some other dependent.

Of course, this is a question similar to the elective manner of filing joint income tax returns in the United States. This is a point that they have and we feel very strongly about and have considered it very favourably.

Of course, once again, it would not be any disadvantage to the economy of the country as a whole, but would be adding to it; more services would be provided and more revenue would be available, and

therefore there would not be any loss of income as a result of this rather small exemption.

MRS. TENCH: I think in fact there would be a gain because there are many housekeepers being paid today who are not declaring their income, and for whom T-4's are not being filed. If exemptions were allowed for those housekeepers, then their name would have to go on record and they would have to declare their incomes and T-4's would have to be filed for them.

MRS. SABIA: I might also add that we have a shortage of nurses; we have a shortage of teachers, and heaven help us, we know of the shortage of teachers. There are many, many women who could go back to teaching if this was an incentive to them, and we need this older, more mature teacher certainly in our economy today, and we are not getting her because there are no allowances for her.

I submit on the economic basis purely of productivity we need these women to go back to teach, to nurse, to be social workers. These are the fields where the scarcity is in our economy, and we think we ought to make it a little simpler for them. We do not want to go to the ends some countries have gone to by providing creches of all kinds from the cradle to the grave sort of thing for children, but we do feel this would be a great help.

THE CHAIRMAN: This would contribute to

the mobility of the female labour force and thus decrease structural unemployment.

COMMISSIONER BEAUVAIS: You say in section 12

"We believe that the actual wages paid to a housekeeper should be allowed as a personal exemption."

That is not the $1000.

MRS. SABIA: No, I am sorry. I think Mrs. Orange meant we would not be allowed to take the thousand dollar deduction. If you were taking the wages as a personal exemption you could not also take the thousand dollars.

MRS. ORANGE: Yes.

COMMISSIONER GRANT: You are assuming the wages would exceed $1000?

MRS. SABIA: Yes.

COMMISSIONER BEAUVAIS: But you would add it into the amount of the wages?

MRS. SABIA: I do not think it is up to us, that limit. We know in our economy what the wage of a housekeeper is, and I think within a certain flexible range we could not state --- we could not say $2000, $3000 or $4000. This is very difficult because things change and the pattern of earnings changes, and I think this is a difficult matter for us to do. I think this is more for a Commission to undertake than ourselves.

THE CHAIRMAN: That concludes the income taxes, I think.

MRS. SABIA: We come to estate taxes. This is another very difficult thing to actually say that this is exactly what we want or this is not exactly what we want. We have in the past said and we reiterate it again the figure of $50,000 true exemption is a more adequate figure perhaps, a more realistic figure than the $40,000 that is now allowed.

We are submitting that the exemption be $50,000 rather than $40,000. This is what we submit here.

Also in item 15 I think it is coupling the two together, so I think perhaps we might treat it together. I would prefer to spend more time on the pension benefits, but I will go over this. Recognition of equality in the marriage partnership. I know this is exceedingly contentious. You can look at it from many angles, and there are discriminations on one side and the other too.

However, we feel that somehow in our taxation, in our Estate Tax Act, there ought to be an equalization between a man and wife. The wife earns we feel and helps, and if we go back to our little stories, certainly she helps the man and vice versa, and I think this should be recognized.

We have asked for recognition in the marriage partnership. I think I would say now

so if the question is asked to me, would you not prefer perhaps, as I think it was the Council of Estate Planning who said nothing under $100,000 should be taxed. We would go along with that, of course, because this is even better I think and because we have studied this, and because the clubs have all passed it and we bring it to you. It is not new. It is debatable.

As I say, I think all of us would prefer to have as the Estate Planning Council said, true exemption or no estate taxes under $100,000. We submit it to you because it has been passed. We feel there should be a weight of equality between the man and wife.

COMMISSIONER BEAUVAIS: On that point would you decrease the $60,000 presently allowed to a widow to $50,000?

MRS. SABIA: No, I think we have said here in No. 16, if you go on, we submit that the present exemption of $60,000 where there is a surviving widow, whether or not she received any part of the estate is not an acknowledgment of equality in the marriage partnership.

We would prefer to have the marriage partnership rather than the $60,000 exemption. In asking for the $50,000 exemption it would mean on all estates even though there was community of property.

COMMISSIONER BEAUVAIS: But you

would maintain the $60,000 exemption?

MRS. SABIA: As it is now, yes.

COMMISSIONER BEAUVAIS: Then you would still have the discrimination you are talking about between husband and wife?

MRS. SABIA: We will concede the point and give you men the fifty. It is the equality we are interested in. How one arrives at the equality is not important. It is the equality. I think we have got to leave behind our old thinking that there is a difference between a man and a woman or a difference in brain power or man power. We have got to recognize equality in our society. We have got to pick the best brains from society; not female or male. We have got to pick the best opportunities from man and woman, and I think it is the sense of equality we are looking for, not so much of how we get that equality.

I am sure a Commission such as yours are in a better position to bring about that equality, and we would not argue with whatever equality you brought up as long as it was equality.

COMMISSIONER BEAUVAIS: In the same section 16, you say the Federal Government has applied this taxation policy in respect of widows in the Province of Quebec. Can you explain that?

MRS. SABIA: In explanation of this, I am sorry it has been worded the way it has been

because I think all of us who are here today are not happy with this wording. We did not feel we should quote Quebec in any sense at all. This is a Provincial matter. I do not think it should be in here.

I think perhaps what we are trying to bring out is the fact that in Quebec there is community of property if you do not have a marriage contract, and the sense of that equality -- we realize there are other facets, and I am not going into the Quebec Civil Code or into their succession duties, but there I think is a showing of equality in this community of property, and I think we did wrong in quoting a province in a Federal presentation. It is in there by mistake and we would ask your indulgence.

COMMISSIONER PERRY: I would like to suggest facetiously there may be a male rebellion one of these days. You may have heard of an American Association of Secretaries and Executive Assistants I think it is called. This is quite a large female organization, one of whose basic propositions is that they do half the bosses' work at the office. His wife claims to create half of his wealth, so this is not leaving very much for the old man to do. I get the impression that I am doing quite a bit myself.

MRS. SABIA: I don't doubt that the day will come when there will be a male rebellion, and probably we will have to give up some of our equality

until they catch up with us. However, we are working within the present framework.

COMMISSIONER PERRY: I think the women are becoming more equal than others.

MRS. SABIA: We are doing more thinking, let us say. Listen to us indulgently.

THE CHAIRMAN: I think there are no more questions on that point.

MRS. SABIA: Now we come to the last and, I think, one of the most important, and that is the exemption of pension benefits from estate taxation.

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This is, I think, an extreme hardship on the surviving spouse when all their lives they have worked and saved to pay a pension or annuity or whatever it may be and find it is capitalized on that wife's life expectancy. Today the life expectancy is 70 and if the husband dies when the wife is 50 that is 20 years multiplied by whatever the pension may be. If it is $2,000 or $3,000 you have already created an estate of $70,000, $80,000 or $90,000. Many, many wives are left with no actual cash to pay the taxes on that amount of money and there is hardship for them to borrow or use that small insurance policy. We find that out in talking to widows and talking to women who have certainly some experience with this. This is a tremendous hardship, this capitalization of pension funds.

I realize the government does not particularly like the words "double taxation". There is double taxation on everything in our society. When we talk of double taxation I think we need to define our terms. In this field the governments are taxing the widow on money she will probably never receive. She might die in five years and she has paid money on something that she will never see, money that she will never receive. I think this is where the hardship lies in the fact of her life expectancy.

I know you have to create an estate and come to the value of that estate and the only way you can do it is perhaps -- I say "perhaps" -- I am sure there are many other ways of doing it but on money or cash that is not actually received. We find it hard to understand that it can be taxed on a life expectancy even though you might die and never receive it.

We feel rather strongly about this point because we have had a number of women who have come to us, members of our own organization and members of others, we have talked to many other women's organizations. We work with the Council of Women, the Business and Professional Women who are fundamentally interested in this too because they can see the wrongs in it for the widow.

Now we have Mrs. McClelland here today. We asked her to come with us today because this is a point upon which she feels strongly and she is one who is typical of the many widows who have had to pay taxes on money that they actually don't receive. Mrs. McClelland, would you add a few words?

MRS. McCLELLAND: My pension was capitalized at $20,983.73 and it brought my husband's estate up to where I had to pay 12.1 per cent on that. In 1956 when my husband died we had to pay everything and I worked it out and it came to a fantastic figure. As far as my husband's estate was concerned I cannot

speak about it politely. However, it was 12.1 per cent. After that for 1956 they deducted from my pension for the year $66.13. In 1957 it was $93. I did get a refund of $41.13 that year and whether that was all from the pension or not I am not sure now. In 1958 they deducted $68.90 and in 1959, $70.20. In 1961 and 1962 they deducted $72.60 each year. That comes to a total, I think, of $517.03. If I live another seven or ten years I will have paid in practically what amounts to a whole year's pension to say nothing of the succession duties I had to pay on $20,983.73. If it had not been for the fact that my husband took out the $5,000 civil service insurance I don't know where I would have been. All his other insurance went into paying for the succession duties.

It was a little bit complicated because he had an estate that was real estate and rundown and it was in trust. It was quite a sum of money and I had to borrow to help pay for the repairs. That had nothing to do with this pension business.

It doesn't take long to pay back a whole year's income at the rate I have been going.

THE CHAIRMAN: Thank you, Mrs. McClelland, for telling me the story. You understand that the most difficult job we have is to try to find equality. I am not sure whether you are suggesting

that all forms of annuities be free from tax.

MRS. SABIA: In Ontario there is an exemption up to $1,200 a year. I think your pension up to $1,200 is not capitalized. Beyond that the whole thing is. Is there any way you can help the person who is getting a small pension? Today $2,000 is a small pension. Could there not be some way?

We are not rigid in the things we are demanding. We are flexible. We would like to get something for the person who has a limited income. A person who has an income of $10,000 from annuities is not as great a concern as the small person who must pay succession duties and has not fluid assets. You see most people provide for fluid assets but not always the small man. The bigger person with the big estate always provides money for succession duties but not the small person. I think we are concerned with the person who is left with $2,000 or $2,500 annuity and it is capitalized on their life expectancy. If there was some way of putting on a certain amount we would go along with it.

THE CHAIRMAN: I think we can understand the hardship that can result.

COMMISSIONER BEAUVAIS: In Section 19 you maintain that future income should not be capitalized, where no capital is receive no estate tax

should be levied. When a taxpayer has during his lifetime purchased an annuity or contributed to a pension plan,thereby investing a capital that will be received after his death in the form of an annuity,then you create a capital that is received by an annuity.

MRS. SABIA: That is debatable.

COMMISSIONER BEAUVAIS: Otherwise a man can invest all his money in annuities and receive the annuity right away and there would be no estate tax. I think the hardship is when a widow would die after four years and she had a life expectancy of, say, 18 or 20 years. Then this is a real hardship. Would it not be advisable to levy that out of pensions and annuities only when received? The amount of tax would be established at the time of death and if it is eleven years that would be one-eleventh paid each year.

MRS. FLAHERTY: We have thought of this. This has been a consideration that would mean a certain proportinn of the tax would come off each cheque and, of course, income tax would come off it too. That would be a more realistic approach. As it is now if the wife dies after five years or remarries all that money is gone. This increases the Federal revenue without anyone receiving the benefit.

MRS. McCLELLAND: I was wondering

whether it would be simpler to charge the husband income tax on his whole salary. I think the amount put aside for pensions is not taxable.

COMMISSIONER PERRY: A lot of husbands would feel very strongly about that. The tax benefit in the deduction is very large. It comes off the top of his income in his earning years.

MRS. SABIA: You would get a hue and cry on that one.

Now we have item 2 which I don't feel we should discuss at all because on April 28th Bill 138 came down in the Provincial House and has been given Royal Assent and there is true exemption. I feel in a Federal submission we should not go into Provincial matters.

We are very, very grateful to you for having listened to us. We know that the tax study is in exceptionally capable hands and we feel very secure that you will come up with recommendations that will certainly be the best for the majority. I think that is what is important, that when changes are made that they are made for the majority of the population. We are cognizant of this matter and we feel very strongly and very gratefully. that you will do a very commendable job and certainly come up with something new, interesting, and with a complete new look. Thank you very much.

THE CHAIRMAN: Thank you. It is good

we are not proceeding to write our report tomorrow for I am perfectly sure we should not be able to restrain ourselves from acceding to everything you put before us. We have not only had a very interesting morning but a very charming one.

Mr. Secretary, have you any other business for us?

THE ADMINISTRATIVE OFFICER: Yes. We have received two briefs which I would like to enter into the record. One is from Mr. G.F. MacLaren, Q.C., of Ottawa. The brief was received into our offices on January 3rd, 1963. It concerns death taxation and the smaller private business in Canada. I would like to enter this as Exhibit No. 88.

---EXHIBIT NO. 88: Brief of Mr. G.F. MacLaren, Q.C., Ottawa.

Also, on May 27th, 1963 we received into the offices a brief from Mr. Archibald G. Smith, a tax consultant of Willowdale, Ontario. The brief is relative to customs duties and sales taxes on pharmaceutical and doctors' prescriptions. I would like to enter this brief into the record as Exhibit No. 89.

---EXHIBIT NO. 89: Brief of Mr. Archibald G. Smith, Tax Consultant, Willowdale, Ontario.

THE CHAIRMAN: Thank you. Those are

now entered.

We will now adjourn and stand over until 9.30 tomorrow morning.

---Adjournment.

ROYAL COMMISSION

ON

TAXATION

HEARINGS

HELD AT

OTTAWA

ONT.

VOLUME No.: 29

DATE: May 29, 1963.

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ROYAL COMMISSION ON TAXATION

Hearing held in the Board of Transport Commissioners Hearing Room, Ottawa, Ontario, on Wednesday, the 29th day of May, 1963.

COMMISSION:

MR. KENNETH LeM. CARTER -- Chairman

MR. J. HARVEY PERRY

MR. A. EMILE BEAUVAIS

MR. DONALD G. GRANT

MRS. S.M. MILNE

MR. CHARLES E.S. WALLS

LEGAL ADVISER:

MR. J.L. STEWART, Q.C.

RESEARCH DIRECTOR:

PROF. D.G. HARTLE

SECRETARY:

MR. G.L. BENNETT

ADMINISTRATIVE OFFICER:

MR. A.J. SIM

ROYAL COMMISSION ON TAXATION

HEARINGS HELD AT THE CITY OF OTTAWA, ONTARIO

May 29, 1963

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Professor K.J. Charles
University of Manitoba.

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---The hearing resumed at 9:30 a.m.

THE CHAIRMAN: Mr. Secretary, are we ready?

THE SECRETARY: We are ready. Mr. Chairman, Commissioners, we have a brief this morning submitted on behalf of the Dominion-Scottish Investments Limited and Economic Investment Trust Limited. Major-General A.Bruce Matthews, Chairman of the Economic Investment Trust Limited, will speak to the brief and will introduce his colleagues who are here with him this morning. I would like to enter this brief into the record as Exhibit No. 90.

---EXHIBIT NO. 90: Brief of the Dominion-Scottish Investments Limited and Economic Investment Trust Limited.

SUBMISSION OF THE

DOMINION-SCOTTISH INVESTMENTS LIMITED and

ECONOMIC INVESTMENT TRUST LIMITED

APPEARANCES:

Major-General A. Bruce Matthews, Chairman

Mr. R.W. Inglis

Mr. H.R. Jackman, Q.C.

Mr. L.W. Skey

THE CHAIRMAN: Thank you, Mr. Secretary. Good morning, General Matthews and gentlemen. Would you be so kind as to introduce your colleagues to us?

I will introduce the Commissioners to you without mentioning names. We would like to know anything you would care to tell us about Dominion-Scottish. It is a public company I think although I am not very sure. You might fill us in on that. We have questions to put to you. There is no need to read your submission as we have all read it and it is entered into the record. You may remain seated unless you wish to stand.

GENERAL MATTHEWS: Thank you, Mr. Chairman. Mrs. Milne, and gentlemen, we certainly appreciate the opportunity of appearing today and making this submission on behalf of these two trusts. As the Chairman has pointed out I am Chairman of the Economic Investment Trust and Mr. H.R. Jackman, Q.C. is Chairman of the Dominion-and Anglo Investment Corporation and other investment trusts. He has joined with us this morning and although the name of his company does not appear in the brief submitted, his company associates itself with these two trusts.

It may be that he would wish to comment on his own behalf, with your permission.

Also I am accompanied by L.W. Skey, on my left, who is Managing Director of both of these trusts. They operate their joint office under a contractual arrangement for the clerical and space and administrative accommodations.

R.W. Inglis beside Mr. Jackman is Secretary-Treasurer of both of these trusts. Beyond these two officers, these trusts have no common connection. This is merely a facility which is attractive from a cost point of view. Both of these gentlemen are available to reply to any questions by the Commissioners which should arise, and I think they would like to comment very briefly on the brief submitted by the Great Britain & Canada, and American Growth Fund Management, if they may, which bears to some extent on our submission.

Now, you have already received the submission from other trusts, including at least one closed-end trust, and we are most anxious to avoid repetition and we have paid some heed to their submissions, of course.

There is a long and interesting history behind the concept of investment trusts as a medium of investment, going back in Europe and more particularly in the United Kingdom with experience in excess of 200 years of proven success. Suffice it to say in Canada this type of investment was first started about the mid-1920's. Economic, if I may use the abbreviated names,was the first closed-end trust incorporated in Canada in 1927, quickly followed by Dominion-Scottish in 1929. It is interesting to note throughout market declines in 1929 and during the 1930's, Economic was able to maintain an unbroken

dividend record. I mention this only as further evidence to support the fact that the closed-end technique or concept has proven itself both in Canada and elsewhere as an attractive form of investment for the individual or the corporation, but particularly for the small investor who is unable to obtain adequate diversification through investment in shares of individual companies.

While I could enlarge at length on the concept of the closed-end type of investment, I would refer to only five of the many features which have contributed to their success and refer to them only in headings. Obviously diversity, both in domestic and foreign securities. Low-cost administrative charges are outstanding in this area compared to other mediums of investment. Constant portfolio supervision, Participation of trust in size, and I mean of the individual investor and at times size is a significant feature in the market place. Finally, the creation of a pool of savings available for investment.

In this latter connection we believe that Canadians have become increasingly concerned about the lack of well-ordered pools of such savings operating in our country. Foreign investors have in fact, through the medium of their trusts, moved in where Canadians have been timid.

Based on the experience of British

and also Scottish -- and they are quite distinct identities in that country -- there is ample proof to suggest the Canadian investor has been placed at a dis-advantage due to restrictive tax practices in comparison with those trusts in the United Kingdom.

I think I am correct in saying the growth of the investment companies in the United Kingdom has been a tremendous assistance to the United Kingdom. There are now 258 such trusts in the United Kingdom who are members of an association, and I know of others who would not be included in these figures. They have assets under administration in excess of two billion pounds. This is a big factor in the economy of the United Kingdom, more particularly in their trading connections throughout the world.

While here there are less than 20 such trusts offering shares to the public with assets of approximately four hundred million dollars -- that figure would be subject, gentlemen, to some modification as it is the 1961 year-end and I have not got the 1962 figure. I should add it includes two major development companies which really could not be regarded as pure investment trusts. I can identify those companies if you wish me to.

Why this wide difference in the pattern? It is the opinion of the trusts represented here that such pools of investment funds are not being used to

the best advantage of individuals or of the investment community in Canada. We believe also that one of the reasons for the relative success of trusts elsewhere has been consistency of tax legislation, whereas the changes and inconsistencies which have been experienced here over the years have inhibited participation by the general public in this proven medium of investment.

In the case of these two trusts, our shareholder loyalty has been reasonably good under these circumstances. However, it is interesting to note the number is not growing, the number of shareholders is not growing. In fact, it would be fair to say it is declining slightly; nor is the capital base being enlarged other than by normal market appreciation, so little new money has found its way into these long-established trusts.

In support of this statement, I should point out the conduit principle which is applied elsewhere has never been recognized by the Canadian tax authorities. In addition to this, our shareholders were not accorded the benefit of the dividend tax credits when first introduced. At a later date, after long representations were made on their part, dividend payments to our shareholders were allowed to qualify. I merely cite these as illustrations -- spread over two or three years each time as some of the deterrent or the type of deterrent that we have

experienced. Accordingly, Mrs. Milne, and gentlemen, it is submitted that the restriction on portfolio management imposed by the 25 per cent limit on income from interest-bearing securities and the further restriction on flexibility which is so highly important in the portfolio administration by the present regulations confining non-Canadian investment to 15 per cent -- these two items create a unduly restrictive limitation on the Canadian investor, particularly when compared to the experience of investors in other jurisdictions.

These two items then form the basis of the recommendation paragraphs of our submission. I hope that you will forgive the brevity of this. I realize that this is a subject which would raise many questions in your mind. We collectively felt it would be better to leave that to your good judgment rather than to try to enlarge on the many features of the concept of the closed-end investment trust which could be put into several volumes.

THE CHAIRMAN: You indicated you are going to preface your proposal to us with what we have already received.

GENERAL MATTHEWS: I would like to ask Mr. Skey and Mr. Inglis to comment briefly on two submissions which you have received in that they do bear on the whole field of investment trusts. Whereas we do not have any quarrel or dispute with either

of these two submissions, you will find a variation in ours, and we thought it should be possibly explained.

It is interesting to note, gentlemen, in Canada there is no association of investment trust companies of the closed-end variety as yet. Otherwise you would have had a submission from them. However, I can report that the incorporation of such an association is now being prepared. Open-end trusts of course have a very large and very industrious association which you have no doubt heard from.

THE CHAIRMAN: This is undoubtedly one of the by-products of taxation that drives people together.

GENERAL MATTHEWS: Yes. May I ask Mr. Skey to comment on the British and Canadian trust brief.

THE CHAIRMAN: If you would, please.

COMMISSIONER PERRY: I wonder if we could clear up just a point of semantics? I notice you are speaking most of the time of investment trusts whereas your brief refers to investment companies. Do I assume you are referring to both trusts and companies in anything that you have said?

GENERAL MATTHEWS: They are similar, Mr. Perry. In 1927 you could still get a title from the Secretary of State incorporating the word "trust"; thereafter you could not. This is now

confined to the trust company as we know it, who is an administrator of estates and so forth.

By the time the Dominion-Scottish applied for their charter the word "trust" had been denied to investment companies. It was merely a matter of nomenclature. The only thing it does for Economic is identify it as the oldest trust, so that it is the same. Their function and role are exactly the same.

COMMISSIONER WALLS: The only thing I was really interested in, since the 1955 Act which made it mandatory for 60 per cent of the gross revenue be invested in Canadian securities was changed, I believe, in 1960 to 85 per cent, what effect has that had on your own particular portfolios? Have you any particulars to show the adverse effect, if any, which you have encountered?

GENERAL MATTHEWS: I have not any figures to support the contention that we were removed from the non-Canadian market. Largely that would be the United States market and the United Kingdom market. The strength of investment trusts is the great diversity, and the success of the British trusts have been world-wide diversity.

I think we can demonstrate to you that under certain conditions of the market we would have enjoyed a more profitable experience had we been able to retain in our portfolio a higher percentage--

for illustration I will say United States securities largely confined to the types of companies which we cannot participate in. The 15 per cent figure we have reached on different occasions and had to hold there.

You see it is our contention, sir, that tax restriction should not be the motivating force in administrating a portfolio. You must stick to the quality, type and location of security. However, I think it would be only fair to say that the tax implications have seriously affected the judgment of Canadian portfolio administrators from time to time in the post-war years.

COMMISSIONER WALLS: Is it not a fact that the 85 per cent has been in effect for such a short time that you really have no adequate bases to know whether over a long period the investor will not be as well off as a high percentage of the Canadian investors?

GENERAL MATTHEWS: We certainly have no mathematical figures that we can produce to prove it otherwise.

MR. JACKMAN: Could I reply to Mr. Wall's question, sir? Because of this restriction of not having more than 15 per cent outside Canada, it makes it so difficult that in one company of about $17 billion in investment trust assets we no longer qualify. It just is not worth our while, and

the question arises is it worth while in our case anyway, having an investment trust or investment company, because the shareholders are subject to taxation in the States -- they are subject to taxation in the company form and then the small residue that is left for dividend distribution in their hands in Canada is again subject to personal income tax.

In other words, you just throw up your hands. This 15 per cent is considered an iniquitous provision of the government. It was done I think I may say at a time more or less in the form of sumptuary legislation to straight-jacket the savings of the Canadian people into the development of Canada. That theory is not quite so prevalent today as it was during that particular time, and to straight-jacket us to 15 per cent is extremely bad.

I should just like to add to General Matthews' presentation on the value of these investment companies in the United Kingdom when war was first declared. Britain had to pay on the barrel-head, and the investment trusts were required -- their assets were commandeered. They had a gentleman in the trust field sent out from Scotland who was resident in Ottawa here and he sold many of the securities in order to pay not only the United States but to pay Canada for munitions of war which were required at that time.

In other words, that it is a good thing for the country to have a certain amount of money available in foreign bonds,and at the present time I think the theory would perhaps receive political acceptance because we are suffering a little bit too much ownership of our own assets, so let us own a little bit of someone else's assets. Does that answer your question, sir?

COMMISSIONER WALLS: Yes.

GENERAL MATTHEWS: May I ask Mr. Skey to comment on British and Canadian?

THE CHAIRMAN: Yes, thank you.

MR. SKEY: Mr. Chairman and Commissioners, in respect of the representations made to you today and previously, I would like to make brief reference to pages 758, 759 and 760 of the transcript of your Commission. These were recorded at your Montreal hearing on the 26th of April, 1963, and contained recommendations of the officers of the Great Britain and Canada Investment Corporation who appeared before you on that day. The first of their recommendations--

THE CHAIRMAN: May I interrupt you just a minute? This is the first time we have had anything before us which sounds like rebuttal, and I think before we proceed with this we had better see if we have imposed any rules in regard to rebuttal. Mr. Secretary, what are the rules?

MR. SKEY: This will not be in the nature of rebuttal.

THE CHAIRMAN: Let me hear why it is not rebuttal.

MR. SKEY: It is a comment.

THE CHAIRMAN: If you agree, we will take it as a comment. I am sorry to interrupt. Will you proceed?

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MR. SKEY: The first of these recommendations is that the Investment Trust Management should be freed of restrictive tax provisions. This is what we support in our brief and it is indeed the crux of all these representations. I would refer to the second, fifth, and sixth recommendations on pages 759 and 760. We have some reservations about them. These reservations are on the grounds of complexity and we agree with the observation made by Commissioner Perry on page 764 when he said they present an administrative chore. While we still believe their implementation would be an improvement on the present tax provisions we also think that the recommendations made in paragraph 7 of page 3 of our brief presented to you today is a better solution to the problem.

THE CHAIRMAN: Mr. Skey, I haven't any idea what the recommendations 2, 5 and 6 are. Do you wish to tell us?

MR. SKEY: Yes, sir. They represent to you that it would be better for the shareholder to be taxed in the long run on the type of income that the trust received. In other words, if 20 per cent of the income was from interest bearing securities, 20 per cent from foreign sources, and 60 per cent from taxable Canadian securities, the individual receiving the dividend from the investment trust would be taxed on the 20 per cent of interest, 20 per cent of foreign

dividends, and tax free on the 60 per cent that came to him from taxable Canadian corporations.

THE CHAIRMAN: Thank you.

MR. SKEY: We recommend a return to the provisions of the Act as it was in 1955. That is to say that not less than 60 per cent of gross revenue from the years shall be from dividends on taxable Canadian corporations. This, we feel, affords a more workable regulation for the Government to administer and the Investment Companies to follow. In other words, we believe it will serve both parties better.

The third and fourth recommendations which have to do with the right to invest abroad and the advantages accorded the Investment Companies, we support wholeheartedly.

The seventh recommendation, which as I understand it, asks for relief from tax incurred through changes made in regulations we also support because portfolio investments cannot be changed quickly and due notice of any tax changes to be made within the period of transition seems to be a reasonable consideration to ask.

Before completing my representations I would like to mention the terms of reference which your Commission has been given and to refer to the request that you propose changes which will encourage the holdings of Canadian equity securities by Canadians.

In giving attention to this part of your findings, I believe that the submissions made to you by the Canadian Investment Trust bear up to consideration because our portfolios are diversified. We are able to hold a higher percentage of equity securities than would be prudent for the individual small investors. Our risks are spread over a broader base than they are able to obtain. Over the past few years these companies which are appearing before you today have consistently held less than 20 per cent of their assets in bonds and have at times held as little as ten per cent of our portfolio in this type of security.

Thank you, Mr. Chairman.

THE CHAIRMAN: Could the comments with regard to the American Growth Fund Management Company Limited be construed as a rebuttal in any way, Mr. Inglis?

MR. INGLIS: No, sir. I think it should be considered as giving support to their brief. At the hearing held on May 6, 1963, Mr. C. W. Goldring, Vice-President of the A. G. F. Management Limited submitted a brief in support of his contention that subsection 69(2)(ba) be replaced by other legislation. These arguments are shown on page 1039 and 1040 of the transcript. I should like to reiterate them to express our support of the five points, which are quite brief if I may.

THE CHAIRMAN: Please do.

MR. INGLIS: Firstly, we do not believe that income taxation is an efficient instrument to control or direct investment flows into or out of the Canadian market.

Secondly, if it was to be used it should apply to all savings institutions and not merely investment companies.

Thirdly, there is no sense in a tax provision which can be circumvented by the simple expedient of changing from a corporate form to a trust form of organization.

Fourthly, under certain circumstances a degree of economic nationalism can be justified, but we believe it is the long-range interest of Canada to encourage a free flow of investments both into and out of this country.

Fifthly, there should be no discrimination between buyers of foreign securities. We maintain there should be no additional cost to the investor investing abroad because he invests by mutual funds which is not present if he is a large investor buying foreign securities on his own.

Thank you, sir.

MR. MATHEWS: Unless Mr. Jackman would like to comment on his own behalf, we have nothing further to add to the brief. In the hope that some questions might arise, we would be happy to answer them.

MR. JACKMAN: I would like to say a word or two because many years ago I was very much concerned with the legislation in regard to these investment trusts and we did at one time -- and here I differ very slightly from General Mathews -- we did have the conduit theory established in our legislation.

We started off first of all with an investment trust, if you like, and it was taxed. The asset or the dividends from which it received income were taxed and when the money flowed to the ultimate shareholder it was taxed. There were three areas of taxation from the same original earnings and that was felt to be an unfair situation and quite an impossible one if you were going to have an investment trust.

An investment trust is simply an aggregation of small accounts that might be in the hands of an ordinary trust company for administration but we believe, following the pattern of the United Kingdom, they are better administered in corporate form and the beneficiaries, if you like, hold shares in these trusts.

The government, when the legislation was first introduced under Mr. Ilsley, in 1940-odd, did adopt the conduit theory of no taxation whatsoever on investment companies, but there were certain rules we had to follow. For instance, that not more than

25 per cent of the company could be owned by any one shareholder. They were not difficult to adhere to. Then the first problem arose when the government in its wisdom saw fit to give 20 per cent tax credit on dividends, inasmuch as some of the income which investment trust received was not in the form of dividends from other Canadian corporations which are, of course, tax free, but came from bonds and some from foreign securities and the shareholder in an investment trust would have received an unfair benefit because he would get 20 per cent tax credit if it were allowed.

Mr. Abbott was then the Minister of Finance and he said "There will be no tax credit on investment trust dividends even though 70 per cent -- 80 per cent of the content of the dividend might have come from dividends from other Canadian corporations."

There we were faced with the first injustice in taking 20 per cent tax credit off our own shareholders.

We went down to see the Department and they were quite agreeable to a proposal, namely, that on that part of the income of an investment trust which was received from sources other than dividends from other tax-paying Canadian companies, the investment trust asked to submit these to 20 per cent tax on that outside portion of income, namely from interest and

from foreign dividends. We asked for taxation. The condūit theory had been formally established.

That went on very well. It was a very fair proposal and went on until 1956 or so. It was pointed out that an investment trust could be formed to hold bonds in Canada and it would pay the 20 per cent tax on them but then that income could be transferred to its shareholders, most particularly corporations, and there would be no further tax.

I will give you the ultimate example: The banks of Canada could have had an investment company hold their investment account and it would have been subject to 20 per cent tax, if you like, but the investment trust, being a Canadian corporation, there was no tax on the money flowing into the bank's coffers. Of course the Government would have plugged the hole within the next year and it was never taken advantage of. It was quite open there but nothing was ever done.

The Government saw fit to make the changes in 1956 in regard to implementing its policy of chanelling Canadian funds into Canadian investments by allowing the investment trust to have only 15 per cent of income from other sources. They also changed the rule in regard to the amount of income which could be received from bonds. I believe it was not more than 25 per cent.

Now, the difficulty of that small 25 per

cent is this, that often you will find bonds will yield you more in this day and age than equity stocks will. You may only get three or four per cent sometimes on bonds, at the present time five per cent -- six per cent, on equities you get sometimes two and one-half per cent -- three per cent, so you can have a very small amount of your money in bonds, perhaps only eight per cent or nine per cent, and it will produce 25 per cent of your income. It works against the proper management of investment companies. We feel this is very unfair and the whole purpose of investment trusts is to provide the small investor with a maximum portfolio, some bonds, some preferreds, and some equity securities which will do his work for him and give him the advantages of constant management and the advantages of certain size.

If we were just doing an operation like the Argus Corporation, or some company of that nature, which is quite different, we would be entirely in common stocks and in the stocks of other Canadian companies. They have no tax problem. Their income is all non-taxable. On the other hand, we feel we must always have some bonds for the protection of the small investor or small savers in this country.

Therefore we believe that both those restrictions on the interest and on the 15 per cent allowed in foreign investments should be done away with. I don't think the Government would look unkindly

at the proposals.

Might I add something to Mr. Walls' point that he made a little while ago about whether the 15 per cent is a restriction. I was over in the States recently and I was interested to hear that the United States government appropriates eleven billion seven hundred million dollars for research which is paid out mostly through corporations under the guise of national defence. As we know many of these inventions are applicable in ordinary life today. Of this amount of eleven billion seven hundred million, one billion dollars is actually chanelled through the universities for more or less pure research.

I point that out as something relative to the whole crux of the national product of our country. With our 19 million people against their 190 million people, we just cannot compete in many areas in the growing field with the United States or with even some European countries.

If we are to do a fair job as investment managers, we must be allowed to invest in their IBM, their Chemical Companies and Research companies. If you have a good idea and can sell it to 190 million people, you can afford to do a great deal of research. In this country you just cannot do it and cannot keep the men to do it.

We are bound as investment managers, we are put under an obligation to invest further and,

as I mentioned, it sometimes seems hardly worthwhile trying to keep the investment trust companies going in this country and to do a good job.

I would like therefore to join with General Mathews and his group in suggesting that the only restriction on investment companies be that not less than 60 per cent of its gross revenue for the year was from dividends from taxable corporations.

THE CHAIRMAN: Thank you. As you and General Mathews have indicated, it is in the long-range interest of Canada to encourage the free flow of investments. I have heard that stated many times before. I would like to know as precisely as possible why you think it is a good idea for Canadians to invest outside their own country? You speak about yourselves as investment managers and in making the decisions you are acting for individual investors. Why is it a good idea for individuals in Canada to invest outside of Canada?

MR. JACKMAN: I suppose because we want to participate in the good things of life and if you cannot set up competition to the IBM, the best thing to do is join them and share in the profits. I am anxious to get back some of the money we Canadians pay to these people. I don't know of any other way of doing it. I cannot suggest how investment abroad helps our country except that it does provide a source of foreign exchange to pay for the imports which our

people are going to get more and more. I would like to say the question is out of the practical. It is out of the dollars and cents area, which is perhaps a little more my field than the general area of what is good for the over-all picture of Canada. I should hate to think that if one were from a small country, one could never participate in the great advances which are being made today in the larger countries that are really spending money on research and doing things in a manner which we cannot hope to follow.

C/ET/je

GENERAL MATTHEWS: May I comment, Mr. Chairman?

THE CHAIRMAN: Yes.

GENERAL MATTHEWS: In addition to the practical aspects Mr. Jackman has mentioned of cash flow and holdings of U.S. dollars or sterling, I really feel that some of the criticism that has been cast on Canada as being too parochial in its outlook with regard to the world trade position can be traced right back to our desire to stay within our own boundaries.

I hate to keep referring to the United Kingdom experience because it is entirely different, but I believe, although this is rather academic, over the long term it is highly important that Canadian money for trade purposes in addition to the investment capital and for psychological purposes should flow in areas that it has never been seen. We want to stimulate every sinew of the Canadian impact on even new countries.

I think it will be a great many years, sir, before we are likely to invest substantial funds on behalf of small individuals in Ghana, but, by jove, Scottish Trust are in there with lots of money. They tie definite situations to the advantage of the United Kingdom trade channels, and this is a factor which we cannot overlook. We are not international-minded in Canada.

I do not suggest this produces a quick answer, but I think it is a very real contribution; these trusts gradually would spread their wings on behalf of Canada in proper proven areas. The risks are greater, but the rewards are sometimes even much greater, so from an academic point of view I just want to add that.

MR. JACKMAN: May I throw in another sentence?

THE CHAIRMAN: Yes.

MR. JACKMAN: We have an example of the Moore Corporation investing in the United States. We have the Massey-Harris, and it has almost come to the situation where if a Canadian wants to have any share in our own oil industry he has to buy American oil stock. Eighty per cent is owned by Americans.

THE CHAIRMAN: Do you wish to add anything to that?

GENERAL MATTHEWS: No, thank you.

COMMISSIONER GRANT: If Section 69 in the past has been used to support the fiscal policy -- I do not say that it has, but the amendments which have been written into the section, particularly the amendment in 1956 where the switch was from dividends to fixed income securities, and then they switched back in 1961 to the 85 per cent dividend in Canadian corporations, might indicate that

Section 69 is regarded as a means of supporting some form of fiscal thinking.

As I understand your companies find that to be unsatisfactory, and that in adopting a long-range investment policy you just do not know quite where you might fit, and there will be changes from time to time from fixed income securities to equity securities, and it is difficult for you to build up your portfolio and maintain your portfolio.

That would be one point you would have in mind, and secondly you would be happy to work under the 1955 arrangement now, whereby 60 per cent of your investment would be in the form of shares in Canadian corporations when you succeeded in getting 20 per cent tax credit for your shareholders, which I understand you now have.

GENERAL MATTHEWS: Yes.

COMMISSIONER GRANT: Could you enlarge any further on that? It has been touched upon, but I do not know that you stated whether or not there was any understanding that there would be a certain amount off your income derived from the dividends in Canadian corporations in order to maintain that 20 per cent.

MR. JACKMAN: I do not recall that there was anything there. One has to refresh one's memory on these things. When I saw Dr. Eaton on the matter, it was just a very nice quid pro quo that the government felt was very fair in the circumstances, and we

had only had, as I recall, one object in view; namely, to get 20 per cent tax credit on a fair basis for the investment trust shareholders, and we did not want them advantaged and we did not want them disadvantaged, so we said that on the income that would not naturally attract 20 per cent, please tax us 20 per cent and let us pass on the remainder of the income to the shareholders as they would ordinarily have it with the 20 per cent tax credit, because it always attracted that 20 per cent tax credit. The sales were absolutely in balance at the time when we paid 20 per cent tax and then passed it on to the shareholders by way of dividend tax credit.

COMMISSIONER GRANT: Do I understand you negotiated, Mr. Jackman?

MR. JACKMAN: I think I had a little bit to do with it.

COMMISSION GRANT: You were in on the Scottish-Dominion --

MR. JACKMAN: Yes.

COMMISSIONER GRANT: What year would that be, do you recall?

MR. JACKMAN: 1955 or 1956, I guess it was.

COMMISSIONER GRANT: It was at least well in advance of the 85 per cent requirement?

MR. JACKMAN: Yes. That last requirement

was under Mr. Fleming's administration. It was too much of a straight-jacket.

COMMISSIONER GRANT: Now I believe General Matthews said that there is no new money finding its way into the closed-end companies, or not any great increase in the amount of money that is coming in. Is that right?

GENERAL MATTHEWS: No appreciable increase, that is correct. I think the practice of these investment companies that have listed or have shares available to the public have been to offer rights to their shareholders to take in modest capital increases, but the fact is that no new investment trusts of this character have been started other than some owned by a relatively small group of people, usually for a special purpose. That would be called the same thing. No new large offerings to the public have been made in recent years, whereas in other jurisdictions they are going on almost monthly; new trusts being developed for creating pools of investment. We have broadened our capital base by issue of rights to existing shares and had increases in capital, but very modest.

COMMISSIONER GRANT: There is quite a number of open-end companies?

GENERAL MATTHEWS: A vast number.

COMMISSIONER GRANT: In recent years. Are they not quite aggressive in the sales field?

GENERAL MATTHEWS: Very aggressive.

COMMISSIONER GRANT: Would you say more so than the closed-end companies?

GENERAL MATTHEWS: Infinitely, because our sales are largely listed on stock exchanges, and theirs are sold through a variety of organizations from door to door.

COMMISSIONER GRANT: And you appropriate your shares --

GENERAL MATTHEWS: Yes, and this accounts for the wide difference in administrative charges. They have a serious loading charge of 8-1/2 per cent and we have none. Our costs of administration, once the fund is established, if you take funds of comparable size, is substantially less.

COMMISSIONER GRANT: Would your loading charge and cost of administration not be one and the same thing? It is only a matter of degree?

GENERAL MATTHEWS: No, their loading charge is paid out in a commission to the salesman.

COMMISSIONER GRANT: Not necessarily applied to the actual cost whereas yours is?

GENERAL MATTHEWS: Yes.

MR. JACKMAN: May I say, Mr. Chairman, in answer to Mr. Grant's query, investment is an odd business in a way. It depends on the amount of risk

which the person can afford to take or the amount of suffering which would be occasioned in the case of loss. The mutual funds -- I happen to be a Director of one of them -- are in a different kettle of fish from this old type of British investment trust. If you want to participate in equities for part of your portfolio, you have your house and insurance policies and so on -- if you want equities, the mutual fund is a very good type of vehicle for you to use, but if you want a general investment portfolio suitable for a person of average means, then the old British type investment trust with a certain proportion in bonds and a certain proportion in preferred and a certain proportion in equities is much more suitable, and it is because of this diversification not having all equities as the unit trusts do, mutual funds mostly -- not entirely, but 90 per cent as a rule or more -- that we run into this problem of taxation.

We want to be a conduit. We are a service organization. We have money for shareholders in corporate form, and they hold the shares of the company and we do the management for them.

In order to compete with a person who puts his funds in the hands of an ordinary trust company, the executor type, he has no problem of taxation at all beyond his individual scope, whereas if he goes into an investment company that is doing

the identical job only in the co-operative form, then he gets into an area of taxation which is bad.

COMMISSIONER GRANT: I understood, Mr. Jackman, that you did not wish to become a true conduit. I understood you would be happy to operate under this section with the amendment or with the Act as it was in 1955, and pay tax?

MR. JACKMAN: We are forced into that position whereas we would much prefer to be a pure conduit. However, the 20 per cent dividend tax credit is a factor which we cannot take advantage of. We cannot ask the government to give it to our people when some of the income which they receive does not naturally attract 20 per cent; namely bond income and dividends from foreign sources. We cannot ask for any special favours, but we want fairness and we are bound, therefore, to submit ourselves to taxation on that portion of our income which does not naturally attract 20 per cent tax credit.

I might just indicate that this conduit theory -- evidence that the conduit theory was accepted. In Section 69(2)(e) there is provision there that we have to pay 85 per cent of our income before the end of the fiscal year, before the auditors come in and tell us what it is, and there are times when it is quite a difficult job, and that is because the theory -- Mr. Ilsley was Minister --

that we are a conduit, but in those days we were changing our rates of taxation rather rapidly, and he was not going to let us be 5 per cent better off by waiting for a tax reduction, or worse off, but we had to pay out income before the end of our fiscal year so that the individual getting it would be subject to the same rates of tax as were applicable during the period the money was earned, which is very clear evidence, and while we have now asked for that provision to be changed, it is a very great nuisance to have to estimate your income before you get it, and pay it out before the end of your fiscal year. Now when taxation is not rising as fast as in the war years, I do not think the government would be unfriendly to allow us as much as three months or so.

If you held a substantial amount, in let us say an American investment trust in a specialized field, and at the end of the year they pay out capital gains dividends, that is taxable to us as part of cur 85 per cent, and you can get hit pretty hard. We had Japanese bonds in one of these companies, and they started paying double coupons when they resumed payments in 1950, and there are various items that come in to swell your income beyond what you estimate, and if you don't pay out 85 per cent, you don't qualify and you are in for a very heavy tax burden.

This is a small point, Mrs. Milne and

gentlemen, but if it could be incorporated in any suggestinns for changes, we would like to have two or three months after the end of the fiscal year to give the officers a chance before we have to disburse 85 per cent of income. Thank you.

COMMISSIONER MILNE: I just want to ask you one question, General Matthews. I think in your initial remarks this morning you spoke about a decline of shareholders, a decline in investment capital which has been apparent in your type of company. Is this a significant factor, and when was it first noticeable?

GENERAL MATTHEWS: I do not think it is too significant at all other than to indicate a lack of interest. I was referring to Economic Investment Trust in particular which has something under 800 shareholders. This amount has been very static. In other words, the popular features of the closed-end trusts have not appealed in the same way that we would like to see them to the middle income group or average investor. I do not know that this would apply to the entire industry.

We do feel the impact of the competition, if you want to call it that, of mutual and open-end funds, and in many instances they are serving as good a purpose but they do not cover off the same wide field generally as the closed-end trusts. It is not significant. This just kind of implies

that the Canadian public have not shown the interest in these forms of investment that we think they should, for the benefit of Canada, to say nothing of the benefit of themselves.

Investment becomes a rather personal thing. I think it is fair to say too that Dominion-Scottish is in the same position, and you may be interested in something that is a little beside the point, that shares of these companies have a real tendency to gravitate to the hands of the very sophisticated investor, the one chap who does not need them, because he sees in them the basis of good experience and much lower cost than he could experience doing it himself.

A high percentage of some of these funds is now held by financial institutions, corporate identities of one kind and another. The thing was not designed for that, for their tax position is a little bit different, but the person you want to attract is the conscientious saver and investor in any income bracket. It doesn't matter.

THE CHAIRMAN: You have not indicated that this matter which Mrs. Milne referred to is caused by tax laws or particular sections to which you object. I would have thought because you say your shares gravitate to the sophisticated investor, it would indicate you are not suffering in this respect because of tax laws.

GENERAL MATTHEWS: Dealers who are in touch with their clients about this tell us when they make a suggestion of participation to a client in an open-end trust, he shies away from the taxable feature at times. We do know this is a deterrent in some instances, and I have a hard time substantiating that. It becomes a sort of legendary thing on the street.

Now, we have touched on a number of features, the 85 per cent of paid-out earnings and so forth that was not in our brief. For example, this 25 per cent restriction on bond holdings and foreign investment, if you get into trouble sometimes the prudent portfolio manager would go heavily into bonds obviously where mutual funds cannot. It has to go along with the portfolio and redeem. We have to live through thick and thin, and we would hate to be penalized on that basis. I think I would be less than frank if I were to say right now that there have been occasions in the last four or five years when our officers would have preferred to have larger holdings of bonds than we want to. In other words, our prudent type of management was somewhat influenced by the fact our tax load would be much bigger.

Fortunately the trend in the securities market gave us a pretty clear indication that this was not long-lived, and we did not feel any disservice

had been done. We would have gone into bonds and paid taxes if necessary, but it is a slight deterrent.

COMMISSIONER GRANT: On the other side of the coin, if investment trusts could switch their security portfolio without any restrictions whatsoever it might well be that in a falling market you could create a very bad stock situation?

GENERAL MATTHEWS: Yes. I think that the one who creates it is the mutual fund because he is obliged to sell to redeem. We cannot redeem our shares. You have to ride with them. We would not be liquiding in the general market unless we transferred to bonds.

Yes, it is possible that we could make an impact, but not to be compared with other holders of securities. It would not be a significant thing at our present size, but you could not deny the fact in theory that this is correct, yes.

THE CHAIRMAN: I have one question. Your proposal that not less than 60 per cent of its gross revenue for the year was from dividends from taxable corporations -- matching that against 20 per cent dividend credit, it would seem to me to be a little out of balance in that 40 per cent is from other sources than taxable Canadian corporations. Is that a fair matching against the dividend credit?

GENERAL MATTHEWS: I think they thought

it was fair when it was originally introduced. This can be subject to some variations. I agree with Mr. Grant that the increase to the higher figure was one of fiscal policy and there was a great desire on the part of all Canadians to channel any money that was being invested into the Canadian scene.

This did create an untenable position for other than emergencies.

I think it would be possible to produce a mathematical formula, but I am of the impression that it is pretty equitable to contemplate 60-40. This was an area that we felt we had all the flexibility that could be normally expected, and the fact is you are not right on those figures all the time; you are gyrating somewhere between 1 per cent and 40 per cent. I know of trust companies who have not appeared before you who hold nothing but equities. That is why they are not here. They are somewhat of a specialized character although they have shareholders, but they are in it in the knowledge that that is their business. I think it is probably fair.

COMMISSIONER PERRY: Your proposal envisages continued taxation of this 40 per cent; you would continue to be taxable on bond interest?

GENERAL MATTHEWS: Yes, at the investment company rate. This is to protect our shareholders. If we went any further we would have to,

I think, expect our shareholders to be denied the 20 per cent tax benefit.

MR. JACKMAN: Actually I think, Mr. Perry, it is 21 per cent. We get into one per cent more -- they throw in another couple of per cents for Ontario. They look upon us as a taxable corporation. We had to do something about the dividend tax credit, and asked to be taxed, but it has gotten us in for a little extra burden.

May I first reply to the question of yours, Mr. Chairman? Is the patient really sick of taxation and why haven't we grown, and if taxation has not held us behind, do we need medication? I do not think it is taxation fundamentally which has kept us from growing.

The shares of all these closed-end investment companies sell at discount. Therefore it is a little bit hard to sell a new share at one hundred cents on the dollar when you can buy the old at seventy or seventy-five cents. They are very rare bargains for people compared with other forms of trusts.

At the moment we are also engaged by the amount of dividend we have to pay out, and if we have to pay an unfair proportion even though it is not large to the government as against an individual looking after his own affairs, then it does weigh against the price at which the trust would

sell in relation to the liquidated value, and therefore against their growth.

GENERAL MATTHEWS: An interesting comparison, Mr. Chairman, if I may refer to it, and I think we are not entirely blameless as trust operators. We are endeavouring now to correct this. In the United Kingdom and in the United States the counterpart trusts in many instances -- not in every one but in a large majority -- have gone up to break-off value, and even in some instances in excess of it. This is particularly true in England where they have never had any tax alteration.

I do not hold ourselves blameless, but I do think one of the contributing factors to our discount which we do not particularly enjoy is the area of taxation which they are free from.

COMMISSIONER GRANT: Would you agree that your shares being diversified, they are likely to find their way into the hands of the conservative investor rather than into the hands of speculator?

GENERAL MATTHEWS: Yes. I think there are other trust investment companies which are not in the hands of the public that are taking a much more speculative view. Two or three smaller ones with only 20 or 30 shareholders. They are really private companies, but for the companies that offer their shares to the public, yes.

THE CHAIRMAN: We thank you very much

indeed for bringing this to us and putting it forward so understandably. Have you anything further you would like to say to us?

GENERAL MATTHEWS: I believe not, Mr. Chairman. We are indebted to you. This is a very important matter to us, but I realize it is a very small leaf in the economy of the whole country which you have to contend with. We are indebted to you for your courtesy.

THE CHAIRMAN: You can be assured we will continue to consider the matter. We will adjourn for about three minutes.

---A short recess.

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THE CHAIRMAN: May we continue, Mr. Secretary?

THE SECRETARY: I have a brief presented on behalf of the Modern Building Products Company of Toronto. Mr. Louis Mostyn, barrister and solicitor, is representing the Modern Building Products Company here and he will speak to the brief. With him is Mr. M. J. Swartz of this company.

I would like to enter this brief into the record as Exhibit No. 91.

---EXHIBIT NO. 91: Brief of the Modern Building Products Company.

SUBMISSION OF

THE MODERN BUILDING PRODUCTS COMPANY

Appearances:

Mr. Louis Mostyn

Mr. M. J. Swartz

THE CHAIRMAN: Thank you, Mr. Secretary. Mr. Mostyn, we have your submission and have read it with interest. There is no need to repeat that operation. We would be very glad if you would care to speak to it and in doing so I would appreciate your telling us a little bit about the company and say anything you wish to say with regard to the brief.

MR. MOSTYN: Thank you, Mr. Chairman. First of all, I would like to thank the Commission for the opportunity to present my brief before them.

I realize it was late in coming and I again thank you for this opportunity.

The Company that I represent is a home improvement company. It is both a manufacturer, distributor and retailer in home improvements and as such has had personal contact with home owners and for this reason is more familiar, or perhaps more familiar with the subject and this is the reason for them presenting the brief. Now as set out in the brief the purpose of my presentation is a submission to the Commission that expenditures on home improvements should be deducted from personal income tax of home owners. There should be deductions allowed on interest on loans for the purpose of home improvements. Deductions should be allowed as a result of municipal taxes directly attributable to improvement of the home of the taxpayer.

Now I realize, gentlemen, that you have read over the submission but I would like to make some comments with respect to it. First of all, in the 1961 census on investigation of the census it was observed there was over 1,181,000 homes in need of repair; in need of major repair, 255,414 homes.

Now, I spoke personally with the census people at Toronto and they advise me that these statistics came as a result of on-the-spot inspections.

Now, the total number of homes in Canada is 4,554,493 homes. This means that 25 per cent

of the homes in Canada are in need of some type of repair.

Now, going down to my second point, the number of homes built before 1920 in Canada now is 1,391,719. Twenty-five per cent of the homes in Canada today were built before 1920. This is a substantial number of older homes. Fifty per cent were built before 1945.

Now, the point which I wish to make here is that there will be an ever-increasing demand as a result of the age of these homes for repairs. The roof is going to go, the furnace is going to go, the outsides are going to go, the exteriors are going to go. A lot of these homes are frame. What has the Government under the National Housing Act done to correct this? They have allowed Home Improvement Loans and the statistics for 1962 indicate 23,895 home improvement loans were approved during 1962 for a value of $42,640,000.

Now, can we compare 23,895 homes to the 1,177,788 dwellings in need of repair, according to the 1961 statistics? Here is a need for Canadians that is quite apparent from your 1961 statistics and I will submit that the figure of 23,895 is infinitesimal compared to 1,177,788 dwellings requiring improvements.

I have made a note here of 66,092 were repaired other than through N.H.A. Even so, this is also infinitesimal compared with the one million homes

in need of repair.

Now, therefore, the brief so given on behalf of my clients is a plea for the home owner, for the individual taxpayer, and for the family which is, in my submission, the foundation of our society. What benefits the individual benefits society and benefits the nation as a whole. I submit that it is the duty of the Government to take any steps possible to avoid any decay of a home, which again I submit is decay of society, and the Government should take all possible steps to encourage better family life through improving the home.

I further submit that due to the decay of a lot of these areas young people are discouraged from going into these areas. One reason is if they sink a lot of money into these homes there is no way of recovering the money, no encouragement or incentive to buy. I would submit that in order to keep the older areas alive and buoyant the deductions I have suggested in the brief be made.

Also I would like to point this out to the Commission that at the present time home owners are discouraged in older areas from remaining there. They are more or less encouraged to move out. Now, why is this? When other homes in the older areas become run down and depreciated, the value of the homes depreciate and as a result the individual living in the older area does not want to put any more money

into the home but wishes to sell. When he sells, who buys? The person who buys is one who must assume several mortgages because usually they don't want to put a lot of money into an older home that is being broken down. As a result the house itself further becomes depreciated and more decay results.

A further argument that I would like to submit is why should the individual, the personal taxpayer not be allowed deductions when businesses are allowed deductions for the same thing? For example, assume a business rents homes, will they be allowed a deduction for income tax for expenses incurred as a result of repairs? Another example, will businesses be allowed to depreciate homes? Will businesses be allowed to depreciate cars? Will businesses be allowed a wide range of expense accounts which increase their personal income effectively? Will businesses be allowed to deduct insurance? Will businesses be allowed to deduct realty taxes? I think you will agree with me, gentlemen, that the answer is "Yes".

I would submit why should the individual not be given a fair break with respect to taxes? Again the basis of our society is the individual, the home, and I submit, gentlemen, that the Federal Government should take the lead in promoting and encouraging improvements to the home, especially in the view that over 25 per cent of the homes in Canada were built

before 1920.

I would submit that every assistance should be given to the individual to help himself, to encourage spending which in turn will promote the home improvement industry, promote the economy as a whole, provide more revenues from which taxation can be ultimately taken, and in effect by giving a deduction to the home owner provide an increase in revenue for the government.

Now, in my brief I submitted that as a result of home improvement at present, local taxes based on these improvements will be increased and this is one reason why many people do not wish to improve their homes. They realize their taxes are going to go up. Any of us who have sat in a Court of Revision will time and time again hear the argument of the individual home owner. He says "I spend money, I try to beautify my home and what happens --- more taxes. The man who does not do anything is the man that does not have any increase in taxes."

My third point in my brief was that although millions of dollars are spent in public housing, I don't think I have to go into the figures, I have the figures here, although millions of dollars are spent on public housing, very small amounts are spent with respect to home improvements. Urban taxes will subsidize slums by no taxation and discourage improvement by overtaxation.

I submit that the Federal Government can take the lead in recognizing the need to society and encourage the home owner to improve his home.

Now I wish to refer to the United States law and I think you gentlemen are all familiar perhaps with the fact that there deductions are permitted in the United States with respect to interest payments.

THE CHAIRMAN: Yes, we know.

MR. MOSTYN: I think that is about all I wish to amplify, subject to any questions.

THE CHAIRMAN: I must say that you have presented this brief very forcefully and ably, Mr. Mostyn. I myself think your submission is perfectly clear and I cannot see any problems in the area of my understanding. I will see if the other Commissioners have any questions.

COMMISSIONER WALLS: You said that all the Government had done to assist the situation in repairing homes was in regard to N. H. A. and not in regard to home improvement loans. Did you deliberately overlook the fact that you are exempt from one of the heaviest taxes, you pay no sales tax on all building materials which could amount to well over a hundred million dollars a year.

MR. MOSTYN: This fact was not gone into in the brief and I must admit this is a concession for the home owner as far as the cost of his materials,

but it is also a concession in fact to the manufacturer. It is my submission that the amount of savings to the home owner is very small. You take a man who is earning four or five or six thousand dollars a year and if he has a large family, or even if he has a medium sized family, many of us are in this position, if a man has to improve his house he does not have very much money left over to improve his home with even with this concession of three per cent.

COMMISSIONER WALLS: It is the Federal Sales Tax of 11 per cent.

MR. MOSTYN: Even so I think you gentlemen will agree with me this concession is not enough incentive to the individual home owner to improve his house becauee he only has so many dollars to spend and if it can be shown that by improving his house he will save on taxation he will be more encouraged to improve his house. In fact, it is my submission that not too many of the home owners are aware of the eleven per cent concession. I think you will probably agree with me on that point.

COMMISSIONER WALLS: Maybe you would recommend that we take that off and take it off their income tax.

MR. MOSTYN: No, I think this should be an addition. The eleven per cent is fine as far as it goes. Even with this the individual home owner only has so much money he can spend. We are not

talking about a huge industry but a man who has a set amount of income and what is an incentive to a man with a set amount of income and what is an incentive to industry are two different things.

COMMISSIONER WALLS: Is it not a fact that the city homes requiring the maximum amount of repairs show up in the 1961 statistics as being held speculatively for sale for business construction with no intention of repairing them?

MR. MOSTYN: The reason that they are being held for speculation is that the areas have started to deteriorate first and they have deteriorated to such an extent that people have found it beneficial to move out and not stay in these urban areas. We will take the slum areas of Jarvis Street area in Toronto. These homes have depreciated to such an extent that the better type of individual has moved out of these homes and the properties have depreciated and as a result it has been beneficial for businesses to come in.

MR. SWARTZ: The primary interest of our company here is we would like to see home owners themselves -- we are not interested in big capital who buy slums or buy large properties --- we would like to see the home owner, the individual be allowed the saving of taxation so that he could improve his home.

COMMISSIONER WALLS: Thank you.

COMMISSIONER PERRY: I wonder if you could clarify the second recommendation. You suggest deductions be allowed on loans for the purpose of home improvement. Did you have in mind the interest on them?

MR. MOSTYN: I would amplify that: Loans and/or interest on loans.

COMMISSIONER PERRY: Is it the interest cost or principal cost that you had in mind?

MR. MOSTYN: I had in mind also the principal cost. Of course, I have to give a wide range for you gentlemen to consider.

COMMISSIONER PERRY: I notice too, your first recommendation is in terms of improvements to the exterior of existing homes. Do you have to acknowledge that the survey was --

MR. MOSTYN: Would probably include interiors.

COMMISSIONER PERRY: Interior improvements too?

MR. MOSTYN: Yes, I would think what has applied to my recommendation for exterior would also apply to the interior as well.

THE CHAIRMAN: Thank you very much indeed, gentlemen. We have considered this and will continue to do so. We appreciate your attendance this morning.

---A short adjournment.

THE CHAIRMAN: Mr. Secretary, I don't want to start the main part of this before Mr. Perry comes into the room. You told me you had a little business, will you get that out of the way?

THE SECRETARY: There was a brief received, Mr. Chairman, in Toronto from Dr. W. Glen Sproule and Dr. Harvey Tonken, B.A. This brief was a short brief and they have asked me to enter it into the record on their behalf, which I now do, as exhibit No. 92.

---EXHIBIT NO. 92: Brief of Dr. W. Glen Sproule, M.D., and Dr. Harvey Tonken, B.A., M.D.

SUBMISSION OF

DR. W. GLEN SPROULE AND DR. HARVEY TONKEN

May 13, 1963.

Income Tax Commission,
Toronto, Ontario.

Gentlemen:

May I give my opinion please concerning the method of taxing professional men, especially practising physicians, which I consider grossly unjust, and possibly harmful to the public's concept of healing, as well as to the general economy of Canada.

As you are no doubt aware, a student undertaking the study of medicine, does so with great sacrifice, particularly if he helps earn his own way through seven long college years. Then he must subsist

on salaries from $25.00 to $100.00 per month for four years or longer, as a resident doctor in a hospital, in order to become competent in a specialty. By this time, he is at least thirty years of age, and probably married. Some have children.

At long last, the young physician, filled with his dream of serving God and humanity, turns to the business of making a living in medicine, only to find during the first year of his practice, that he is expected to open an office, buy equipment, take care of the basic requirements of his wife and children, pay off all his accumulated debts to parents and others, and on top of everything else, pay a huge proportion of his income to the government. Obviously he can save nothing. It is usually five years before a young doctor is out of debt. By this time, he is thirty-five years of age, and because of all his expenses, he is forced to look carefully at this business side of his profession. He compared himself to the engineering student who has been earning his high income since 23 or 24 years of age; to the dentist, who has had only four years of university training compared to his eleven. Is it any wonder, then, that a good many doctors, realizing that they have only a few years left to work, become mercenary minded, and devote themselves to getting ahead financially? This is not fair either to the doctor, who began with such high ideals, or to the patient, who readily sees that his doctor is making

unnecessary house calls in order to make more money! Instead of the doctor's life becoming a joy in serving God and humanity as he had envisioned, he finds himself caught in a race to catch up with never-ending expense. Most doctors have to borrow money from the bank to pay their income tax during their first five years of practice.

May I suggest that the following be considered for all university graduates, but most particularly for doctors:

1) that the physician be allowed the first two years after graduation to be completely income tax exempt, as this is his lowest time of earning power.

or

2) that a university graduate be graded according to the number of years he has spent at university studying, e.g., so that the first year working, he pays a small proportion of his income, the next year a little more, etc. -- until finally he is paying his full share, when the number of years is up.

With thanks for your consideration,

Sinerely yours,

(sgd) W. Glen Sproule, M.D.

(sgd) Harvey Tonken, B.A., M.D.

THE SECRETARY: I have one other item. You will recall, Mr. Chairman, that Professor Carl Shoup and Mr. J. van Hoorn gave evidence before the Commission on March 8. A summary of this has been

prepared by the editors of the Commission staff and I would like to enter this summary into the record as Exhibit No. 93.

---EXHIBIT NO. 93: Summary of Evidence of Professor Carl Shoup and Mr. J. van Hoorn.

ROYAL COMMISSION ON TAXATION

Report on discussions between

Mr. J. van Hoorn
Executive Director of the Bureau of Fiscal Documentation
&
Professor Carl Shoup
of Columbia University, & U.S. Member
E.E.C. Committee for the Harmonization of Taxes
&
Members of the Commission

held at Ottawa, Friday, March 8th, 1963

Commissioners Present:
Kenneth LeM. Carter, Esq., Chairman.
J.H. Perry, Esq., Acting Chairman.
D.G. Grant, Esq.

The object of this discussion was to to gain as much first-hand information possible about the tax problems faced by the European Common Market countries (E.E.C.) and in the seven countries which comprise the European Free Trade Area (E.F.T.A.). It was hoped, when the Common Market was formed, that the progress made in the gradual harmonization of taxes among these widely divergent economies would be of acute interest to a body studying the tax structure of the Canadian Federation. Moreover, as Europe presents one of the most rapidly growing groups of national economies, Mr. van Hoorn and Professor Shoup were asked specifically whether tax measures had helped or hindered this progress.

Both Professor Shoup and Mr. van Hoorn were agreed that, considering the complexity and extent of the various national and international tax systems, surprisingly few studies of any depth had been made. The National Economic Development Office (NEDL) in London was a beginning in that country, and work was being done in French Universities and by the Italian Government, who have used tax measures to promote growth in southern depressed areas. In Germany also there was an awakening to the needs of counter-cyclical policies. Moreover, the Netherlands and Belgium Governments were acutely aware of fiscal policy as an economic weapon. But in Europe, with its rapid role of growth and burgeoning economy, the need had been rather for a

brake on inflation than an accelerator for development. It became clear, however, that such moves as had been made, had not produced the detailed data on European tax structures and economics which are needed for accurate study.

Professor Shoup confessed that in view of this and the size of the economic problems, economists were reduced to a high level type of conjecture about the effects of tax measures.

Passing to specific taxes imposed, Mr. van Hoorn questioned whether Canada could learn very much from Europe. He pointed out that many recent measures introduced into Europe have been or still are present in the Canadian tax structure, and suggested that, rather than Canada learning from Europe, it might be the other way round. Moreover, Professor Shoup agreed that most Europeans do not regard their tax structure as a major factor in their growth, and that while North Americans think that the European tax system has been a paramount growth factor, this view is not so prevalent in Europe. Coupling this with the acute lack of empirical work upon incentive legislation, it early became apparent that though Europe was making great strides towards a certain amount of unification of its taxes, its problems of cascading turnover taxes, hidden excise subsidies and so on, were very great. The nearest parallel to the Canadian scene would be if every province collected different income taxes and had

separate excise tax barriers.

Mr. van Hoorn then stressed the complicated nature of most of Europe's tax laws. Many, he said, originated during the First World War and were, therefore, showing signs of strain in view of the rapidly changing commercial structure of Europe today. Nor were efforts to modernize them always successful. Everyone was very happy to see the old Belgian laws replaced by a new system, but it is so complicated that no one can understand it.

Personal and Corporate Income Taxes

The taxes on personal and corporate income were then discussed in detail. On both of these the methods of taxation varied radically, but all countries had a tax on total income of residents and the domestic income of non-residents. In the corporate field, the picture was infinitely more complicated. France, Luxembourg, The Netherlands and Germany imposed, with certain minor variations, a flat rate on both resident corporations and on the domestic income of non-resident corporations. Italy suffers from an antiquated system of "schedular" taxes on various categories of income at different rates. The U. K. has a profits tax on total income and Switzerland has a federal structure of taxation, with levels of tax imposed by the Federal Government for defence, by the cantons (provinces) and municipalities, in varying degrees.

(In Canada, corporation law,

providing about one-fifth of the Federal Income, is about 20 per cent of the first $25,000 and thereafter about 50 per cent.)

Net Worth Tax

The next point covered by Mr. van Hoorn was the imposition of a tax common in Europe, but not found here in Canada. "Net worth" tax originated at the end of the last century in Germany. It is a capital levy on both individuals and corporations and was found in Germany, Luxembourg and The Netherlands, but in the latter country only on individuals. The Swiss cantons impose a net worth tax on individuals and corporations while the Italians have a net worth tax on corporations. Also net worth tax is found in Scandinavian countries. In answering questions upon this tax near the end of the day, it became clear that one of its advantages was that net worth tax could maintain spending by bringing hoarded cash into play. Secondly, if it is desired to favour labour income, as opposed to unearned income, instead of giving earned income exemptions, the source of unearned income is taxed. It is, therefore, unnecessary to give exemptions for earned income. Mr. van Hoorn made it clear that opinions in Europe on the merits of this tax were divided.

(Net worth tax does not exist in Canada, nor does any tax on

capital gain, as opposed to capital, although judicial interpretation of "capital gain" has been narrowed in past years.)

Taxation in Federal State

Of acute interest to the Canadian Federal scene were Mr. van Hoorn's comments on federal taxation matters, both universally and within the federal states of the E. E. C. He admitted that federality was one of the most controversial elements in Europe today, as it always has been in Canada. While there is nothing comparable to the Canadian situation, it was heartening to note that others shared our general problems. Switzerland particularly, where the cantons have the exclusive right to levy direct taxes, the Federal Government is kept to a low budget by the limits of its taxing powers.

Germany is also a federal state comparable to Canada. The German states have considerable revenue raising powers of their own, and are entitled to two-thirds of the income tax revenue. Moreover, in all these countries, there is a feeling that taxes within the E.E.C. are complicated enough, without adding the spice of Federal Provincial relations. There is, therefore, a growing movement towards centralization. Mr. van Hoorn put forward the view that it is realized in these countries that fiscal and stimulating economic policies can be thwarted by too much

local autonomy in taxation affairs.

(In Canada, the power to tax is divided between the Federal and Provincial Governments by the B. N. A. Act. The Federal has unrestricted powers; the province may raise money by direct taxation within the province for provincial purposes. This latter has been extended enormously by judicial interpretation.)

Incentive Taxation

Incentive taxation was then exhaustively discussed. It was admitted at the outset that while many measures had been taken in this field in several European countries, there had been little analysis of results. Taking his native Holland as an example, Mr. van Hoorn stressed that the transition from a principally agronomic society to an industrial one had been aided, -- at least so far as anyone could tell, by extensive incentive tax measures. Moreover, in Germany, taxes were used to foster the building industry to help restore the devastations of war. Most of these incentives, however, were dropped during the 1950's. One method which was used extensively in Germany was to split the rate of income tax upon corporations. The prime purpose of this was to stimulate the distribution of profits. It was a simple scheme whereby distributed

profits were taxed at a significantly lower rate than undistributed profits. The success of this measure has been challenged, however, on the grounds that the capital market in Germany is still very poor. German shares are difficult to obtain and unpopular.

The favouring of certain geographical depressed areas has also been tried in Europe, but it is regarded as discriminatory, and difficulties of application are immediately apparent. Only in Italy has any extensive work been done by the Central Government, and no studies are available to show whether their work has been beneficial. In the U. K., where the problem is acute, little has been done in the tax field, and in the U. S. it is constitutionally impossible.

(In Canada such methods have been recently instigated, allowing special capital allowances for investments in designated depressed areas. The results are as yet uncertain.)

Special concessions for small businesses have been made recently in the E. E. C. Prior to that time, by merging, small businesses were liable for heavier taxation. The new concession in France allows small businesses of capitalization under about $10,000 to establish a holding company for research purposes.

Double Taxation.

The discussion of small business and

big business raised the topic of double taxation on an international as well as a national level. This has proved one field in which great efforts have been made to use taxation to implement Government policy. But here again, expert opinion on both sides of the Atlantic is radically divided on its incidence, particularly on the extent to which corporate income tax is passed on to the consumer. In Europe it is not generally accepted that it is passed on at all. In Canada it has been said that as much as 95 per cent of the tax is passed on to the consumer through higher prices.

Mr. van Hoorn explained that the general situation in Europe was that there were taxes on both corporations and shareholders, and to say that there was no double taxation in countries like the U. K. is a fairy tale, because although there is no double taxation in the limited field of income tax, surtax and profit tax take ample care of the situation.

The most interesting example in Europe of attempts to deal with the problem is found in Germany, where the rate of corporate income tax is 51 per cent, and that on distributed profit only 15 per cent. This split rate has been recommended as the best solution to the problem of double taxation of companies and their shareholders. Similarly, this device also solves other problems. Notably, it will increase the flow of investment capital into channels where it is most needed, thus materially assisting the capital market.

Mr. van Hoorn explained its implication in detail and dwelt on the dangers of this system, particularly in the situation where the parent company is outside Germany and the subsidiary is German. This means that the subsidiary can distribute profits at the cheap rate and then loan money back, so that a 36 per cent (51 per cent - 15 per cent) tax rate can be gained.

A second abuse of this system is that many German companies can establish a holding company abroad and have German profits distributed to such a holding company. Thus, all German profits would be taxed at the lower rate. Mr. van Hoorn put forward the view that the German system would be less liable to abuse if the results of double taxation were reduced by a tax credit system whereby shareholders would be entitled to a credit for corporate income tax against their personal tax. Examples of such a credit are found in the U. K. and under the new Belgian Income Tax.

(A form of tax credit system is already in operation in Canada. A tax credit of 20 per cent of dividends paid by Canadian companies is deductible.)

<u>Corporate Accumulation</u>

The speaker then dwelt briefly on the taxation of corporate accumulations. This is not a uniquely European situation, nor does it present

particular problems, save in abuses arising from holding companies where tax treaties are favourable. Measures have been taken to prevent this, but, in general, except for the surtax in the U. K., no provisions exist against the accumulation of profits.

Family Income

The family income field, the Commission discovered, is radically different in Europe from the situation in Canada. In most European countries the income of the family is pooled, the breadwinner paying all the tax, even if he is not working. It was admitted by Mr. van Hoorn that it was thus cheaper to live in sin and, therefore, in Germany many young people weren't marrying. This lead to government action to split income tax. In England and Holland, the married woman has a larger deduction for earned income which helps even out this inequality.

(In Canada, married couples are taxed together, unless the wife makes over $1,250, in which case each can file a separate return.)

The Work of the Neumark Committee

At this point, Professor Shoup lead the discussion on to the work of the recent Neumark Committee, and explained in detail some of their findings. The Committee was composed of academic personnel, set up by the Commission of the E.E.C. about two years ago to study public finance. The terms of reference of the Committee were to discover what aspects of the present tax system in Europe would distort competition in the Common Market and how tax barriers could be eliminated. It was recognized that a discussion on this point would be beneficial to this Commission only in certain restricted areas. In fact, Professor Shoup stated that he would leave the relation of the Neumark Report to Canadian affairs to other hands. Although the topics discussed by Professor Shoup were essentially practical and although they contained little, if any, theoretical content, his comments proved of value nonetheless to the Commission. The Neumark Report spent much time examining the practical problems arising from tax barriers between countries and while this bore little relation to the federal-provincial tax structure in Canada, it was of interest from the point of view of Canada's relations with other countries.

Under the universal European system employing the destination principle, each country

grants exemption on its exports from the sales tax, and taxes imports and domestic goods at the same level by a domestic sales tax.

Various methods of avoiding tax barriers were discussed, such as the concept of the floating exchange rate and the obvious advantages inherent in the truly interior Common Market concept in which there are no excise barriers at all. It was, however, realized that from the European point of view both of these solutions were totally unrealistic. Another solution is the imposition of a heavy retail tax. However, the committee were of the opinion that while the public might accept a 5 per cent tax, to double or triple it would be asking for trouble.

Value Added Tax

The main recommendation centred upon the value added tax which is already, albeit with some difficulty, applied in France. The principle is in theory appealingly simple. A tax is imposed at every stage in manufacture and distribution. The manufacturer pays a tax on the finished product from which he may deduct the taxes paid during previous stages of manufacture or distribution. The advantage of this plan from the Canadian viewpoint is that it is neutral in its effect as the amount of tax will be the same however many stages the goods pass through, always provided the net sales prices are the same.

A further advantage is that in its administration each level of taxation assesses the previous one.

However, Professor Shoup did not dwell upon some of the difficulties of administration and of the collection of this tax. Certainly the French experience has not been altogether happy. However, it became clear that the new concept of the "value added tax" was becoming highly regarded by European economists.

The Chairman expressed the view that rather than glean more factual information from the two experts, the floor should be thrown open to members of the Commission to ask questions on general policy and trends in Europe today which might have bearing on the Canadian scene.

Personal Tax Rate Structure

The first point to be raised was whether there was opposition to the exceptionally high rates of personal income tax in the higher income echelons. Professor Shoup felt that the issue was not between proportional and progressive personal tax, but between progressive tax with loopholes and progressive tax without loopholes. He felt that even those suffering high rates were happy to bear it as long as escape hatches were preserved.

Capital Gains

The distinction between capital gain and income was the next point raised. This has been the

subject of much litigation in Canadian courts, but Mr. van Hoorn said few cases had arisen in Europe. However, Germany and Sweden have developed rules relating to the time lapse between purchase and sale similar to those in use in Canadian courts.

(As has been said, Canada has no capital gains tax as such but people who buy real property, if sold quickly and at large profit, are looked on with suspicion. e.g. see Regal Heights case (1960) C.T.C.46.

Net Worth Taxation

Professor Shoup was asked why European economists have shown so much enthusiasm for this method of taxation. While he admitted opinion was divided on its merits, be repeated some of Mr. van Hoorn's arguments and added some of his own. First, it is an inducement to put money to work. Secondly, one way in which a higher tax burden can be placed on investment income is to tax all incomes earned and unearned alike at a similar level. A net worth tax can then be imposed separately which will, in effect, be a tax on unearned income. However, one point did emerge. It is impossible to get tax rebate on net worth. On income tax, it is possible, which might mean that income tax was the more conducive to risk taking.

This lead naturally to a discussion of the so-called tax on apparent wealth. Many stories have been heard, especially from Italy, about people paying tax on the sort of car and house they have. This point was soon cleared up however. It is not a capital levy, but these facets are merely used to indicate income.

Another important aspect of net worth tax was then mentioned. Professor Shoup suggested that it could with advantage replace death duties. The concept of death duties in legislation in Canada is based on an attempt at redistribution of capital wealth and the prevention of enormous estates being passed on by inheritance. Trusts and gifts inter vivos, however, have left the ideals of wealth distribution inherent in the death duties taxation very tattered indeed. Moreover, a net worth tax would tax the present generation rather than future ones. Legal complexity is also reduced. Doubts were expressed, however, on the possibility of the imposition of such a tax. It was felt that there would be much hostility from the public towards a tax of this nature, and since the amount of revenue raised by death duties is relatively small, the trouble caused by such a tax might be more than the tax was worth.

(The estate duty in Canada and the Capital Gains Tax in the U.S.each only raise about 1 per cent of

national revenue. A separate department of the Federal Government is needed to collect this tax because of its complexity.)

Value Added Tax

As has been mentioned above, the concept of the value added tax was somethimg new to Canadian economists, and the Commission returned to this topic. Professor Shoup was asked what criticism had been made of it.

He pointed out that if one disapproves of heavy sales tax, then one disapproves of value added tax for the same reasnn. One criticism which could be levied was that it had to be raised from a large number of manufacturers, distributors and so on with the attendant administrative costs. Although the French value added tax was extended and refined during the 1950's, world experience of the value added tax has not been greatly encouraging. In Michigan where there is a business receipts tax similar to the value added, it has suffered from amendment and truncation. The only conclusion Professor Shoup drew from this is that the tax is more aptly used by national or international bodies than by state or provincial legislatures.

This immediately brought the value added tax into a different perspective from the Canadian point of view. A member asked whether, on

the subject of the value added tax, an analogy could be drawn between the regions of Europe and the economic regions of Canada.

Death Duties

Death duties in Europe were then examined. Mr. van Hoorn felt that only Switzerland offered an attraction as a domicile from the point of view of death duties. In Europe generally, the death duty taxes varied radically. In Italy, two taxes are levied, one on the estate, the other on inheritance. He than mentioned that valuation at time of death was general for stocks and shares, but the valuation of a life interest under a trust -- a legal concept foreign to continental lawyers -- was very difficult indeed. However, the problem is much less than in countries governed by the common law.

(Canada has inherited in nine of the provinces the common law concept of trust. While no "trust" exists under Quebec law, it is simple for a Quebec resident to set up a trust in another province.

Depreciation Allowances

The LIFO system is now generally accepted in Europe for inventory valuation. Elaborate schemes have been adopted to deal with the problems of depreciation allowance in connection with industry

since few governments can admit inflationary tendencies in their currency.

Business Expenses

Mr. van Hoorn stated that most European countries were generous with expenses, even those unrelated to income, such as legal costs. There was a movement following the States to tighten up on expenses, in Germany, Italy and France.

(No comparable clamp down on expenses has yet occurred in Canada. There is reasonable tolerance, provided always that the expenses are incurred in the earning of income. e.g. only various headings of legal expenses are deductible.)

There was, unfortunately, no time to delve in any depth into the problems of the relationship between government and business losses. However, it was agreed that Government attitudes towards profit and loss showed large areas of inconsistency, but a prima facie case could be made for Governments sharing in losses as well as profits in some areas of business.

THE SECRETARY: Mr. Chairman, we now have a brief presented by Professor K. J. Charles, Assistant Professor, Department of Economics, University of Manitoba. This is a person brief submitted by Professor Charles who is going to speak to it this morning and who tells me that his Department is aware and his University is aware of this brief. I would like to enter it into the record as exhibit No. 94.

----EXHIBIT NO. 94: Brief of Professor K. J. Charles.

SUBMISSION OF
PROFESSOR K. J. CHARLES
ASST. PROFESSOR OF ECONOMICS, UNIVERSITY
OF MANITOBA.

THE CHAIRMAN: Thank you. Good morning, Professor Charles. Thank you for your submission to us and for coming here today. Your brief makes extremely good reading, I might say. We have all read it and there is no need to do that again. I enjoyed every bit of it and thank you for it. I assume that you were prompted to present this brief because of your interest in taxation and because you are an economist and you are teaching at the University of Manitoba. Would you care to tell us something about your qualifications and also if you would like to summarize your submission or speak to it.

PROFESSOR CHARLES: Thank you, Mr. Chairman. I am grateful to you for affording me this opportunity to appear before you. May main motive in presenting this brief was to represent the viewpoint of the economic theorist. I am aware from public pronouncements and various editorials that have appeared in the public press that there is a great clamour for reduction of taxation in Canada. I am not convinced that reduction of taxation by itself will herald an era of rapid economic development and growth. I believe that taxation has a positive role to play in economic growth as yet. I think this view should not go unpresented.

I think the economic theorist is conscious of a gap between economic theory and economic reality. I think he feels this gap at two stages. First, he is conscious of a gap between economic theory and the theory of economic policy. There is a tendency in my profession, I am afraid, to spend a great deal of time building elegant economic models without often trying to see to what extent these models are applicable to economic reality; therefore this type of gap develops in economic theory.

A second gap, which I would say is even more serious, is the gap between the theory of economic policy and the policy itself, largely because policy is not in the hands of the economist and he is quite aware of the fact that what may seem right from the point of view of economic theory is not put into practice simply because it is not acceptable to the public or

to the effective section of the public.

In the case of the contributions made by James Keynes to depressions now I think it is generally accepted capitalist society has been saved from very serious crises because of the application of Keynes policies.

I think due to the passage of time and due to the fact that in the world we are confronted with new problems we are now entering an era when the crisis faced by capitalist society is not a simple one to merely maintain full employment, but rather that capitalist society can maintain a stable and high rate of economic growth.

This, I think, capitalist society presently faces, and for this the mere application of Keynes' policy would be inadequate because it would deal with short term problems of maintaining full employment. Keynes' theory was related to what you might call a closed model. It did not take into account the various repercussions on the economy such as international trade.

In spite of the continuous application of Keynes' policies, Canada has been continuously through the last several years confronted with the problem of rising and persistent unemployment.

I would submit the reasons for this are mainly the following: On the one hand you will experience, as shown if you apply Keynes' policies, rising prices and this affects international trade and imports rise very rapidly, as can be

seen in Canada in 1956 when there was a sudden spurt in imports. All this has a very serious effect on the balance of payments of the country. Therefore, Keynes' policy has to be chopped off prematurely because we are dealing with not a closed but open economy.

Another factor is the fact that while the very success of Keynes' policy is in its application, it introduces an element of inflexibility in the economic system.

There was a time when the business man could not be sure of proper policies by a Government to combat depressions, say of the dimensions of the one we had in 1929, and therefore prices had a fairly high degree of downward flexibility in depression or inflation.

Today the economy is assured of a certain level of aggregate effective demand. Therefore there is not the same incentive to reduce prices. This is further enhanced by the fact that we have not highly competitive industries and firms in the economy but rather very large types of industries and firms. When you pursue Keynes' policy and increase effective demand in times of unemployment this does not bring about the consequence which Keynes' policy could, assuming an economic crisis, by a high degree of production. His theory is the people will demand more entertainment and more entertainment, more clothes and more goods and those will be produced because of the highly competitive nature

of the economy.

Our modern economy does not have this high degree of competitiveness with the result that when the Government implements Keynes' policies, total effective demand will demand more goods and services; but the incidence of more goods and services produces a situation which would bring more people into employment, industries raise prices on the commodities and, therefore, I think this is one of the reasons for the severity of some of the crises we have had in recent times.

We have the spectacle today of overall lack of effective demand combined with an inflationary situation so that this, I believe, is the reason why many persons applying Keynes' model, without taking into account all the factors which I referred to, have tended to say "What is the necessary restriction on the monetary policy and fiscal policy?"

I believe society is confronted with the situation that at the same time there is overall lack of effective demand. Keynes' policy requires we should increase effective demand but with increased effective demand drawing more people into employment we find prices going up. This is a situation in the simple Keynes' models.

A third factor is the fact Keynes' policy says "If you want to have full employment total effective demand should be of the magnitude that all persons are drawn into employment." Keynes' policy did not set the economy in the text of a time dimension.

What happens is when a certain amount of

capital is forthcoming this increases the capacity of the nation to produce. Therefore it is not ensough if in 1960 we maintain the same effective demand we had in 1959. We need continuous increase in the total effective demand of society. We need continuous increase in the growth of the economy.

Here we are confronted with the problem in Keynes' policy. This belongs to the realms of post-Keynes' economics. It has strived to present dynamic systems to analyse the problems of our society.

Here we find a certain feature as a paradox of growth. Namely, in times of scarcity of capital business men want to invest more. That seems the profitable thing to do. When investment takes place at too rapid a rate the economy is not able to keep up with it, especially because of leakages through international trade. The total effective demand does not keep pace with the effective demand necessitated by the large increase in the productive capacity of the National so very soon the high rate of investment leads to excessive capacity, the economy is characterized by excess capacity.

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Here, the private entrepreneur, naturally in such an environment, has no incentive to invest more because, from the point of view of the marginal calculus of the private entrepreneur, it is not desirable to invest. On the other hand, it is precisely the time when more investments should be forthcoming so we have a paradoxical situation of requiring more investment precisely at a time when capital is scarce; we have to build more factories when factories show excess capacity; we have to curtail building when we find that capital is scarce.

This is one of the important features of the dynamic system, and this, I submit, requires, too, control of the volume of investment. While it is desirable, from the long-term point of view, investment should be continuously growing.

It is highly important that short-term spurts in investment should be avoided; excess investment, I should think, is not desirable for any short space of time, especially the growth of investment that the Canadian investment had in 1955, 1956, 1957. This should be avoided, and it seems to me that the policy implication of this is depreciation allowances will be necessary in times when it is in the long-term interest of economy that investment should be encouraged. While depreciation allowances, from a static point of view, may not be desirable, from a dynamic point of view the economy requires more investment precisely at the time when private enterprise is not willing to invest more because it is contrary to the immediate interest of private

2 enterprise.

From a long-term point of view, if action of this sort is taken, this will encourage growth of the economy and private enterprise will benefit by it because this is something that should follow from the projection of the collective actions of all entrepreneurs, and this is where the Government is in an advantageous position in this regard, and when this is done the economy can be made to maintain not a high but a steady rate of growth.

The other point that I had made: what is desired is not investment per se but rather growth of the economy. I certainly am conscious of the fact that investment is only one element in the economic growth, and I am not sure it is the most important element. A number of studies have shown that it is the technological progress which is the more powerful propellent of economic growth, and therefore our economic policy should be not simply to encourage investment per se but rather to encourage economic growth.

For this I submit we require the very great encouragement of technological progress in society. Technological progress, of course, is not a term which can be analyzed very easily because it is something much more intangible than capital investment. Capital investment often goes hand in hand with technological progress, but I think the policy makers should be conscious that although technological progress is important, education, research, all play a vital role in our economy.

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There is now a recognition of the very high importance that technological progress, research and education have in the economic growth. For the last several years most of the economic people have been treating investment as the sole generator of economic growth. This is, however, being corrected, and I would like to see this corrected in terms of economic policy, as it were.

I think, Mr. Chairman, this is the burden of my song.

THE CHAIRMAN: Thank you, Professor Charles. We have some questions for you. For myself, I would like to refer to something which you just mentioned: the fact that prices had gone up, or, at least, had not gone down by virtue of lack of competition, restrictive competition. I think it is the experience of foreign investors, investors in Canada, particularly those who have, in fact, started their own companies in Canada, they have found it to be a pretty competitive market, and in many cases these people have not been successful because of the very high degree of competition in Canada.

I would think, if we look at statistics of company profits over a period of years, we would see that they have gone down in relation to sales, thus indicating, I would suspect, an increased inefficiency of distribution, perhaps, or manufacture, and, of course, I think they have gone down in relation to capital. Perhaps the best measure of that is the price-earnings ratio we see imposed in respect of shares trading on the stock market.

I was curious as to why you would make a point

4 that prices have either gone up or not come down as much as might be expected.

PROF. CHARLES: Well, I think that in the Canadian economy there are a number of forces operating which have prevented the transformation of the Canadian economy into a full-fledged manufacturing nation. I would say statistics show that in the decade 1950-1960 the manufacturing sector of the Canadian economy has not registered really rapid growth.

THE CHAIRMAN: I beg your pardon?

PROF. CHARLES: Has not registered really rapid growth. It has been growing at a rate of three or four per cent. This, I would submit, is unsatisfactory. We are aware that development of the manufacturing industry could absorb into employment the increasing population of the country, so I feel the growth of the manufacturing sector of the economy was not satisfactory.

This is, perhaps, complicated by the fact that foreign interests, when they establish in Canada, they have their eyes mainly glued to the domestic market. Many of them are established by parent companies, and they establish here expressly for the purpose of competing in the domestic market. This, I think, is not in the best interests of the development of the economy in that we feel it is an impediment to the development of Canada's export trade.

A substantial segment of the industry is geared completely to the domestic market, and therefore its sights are not turned towards foreign markets. This, I think, exercises a lack of the growth of the

5 Canadian export trade.

THE CHAIRMAN: That is a disability in regard to capital. However, I would suggest, on the other hand, it does provide employment and as such it is useful to the Canadian economy.

COMMISSIONER WALLS: I have some questions on a later part of your brief. Are you going to enlarge more on your brief?

THE CHAIRMAN: I think Professor Charles did not expect to say anything more from his brief except to reply to questions; is that right?

PROF. CHARLES: Yes.

COMMISSIONER WALLS: I would like to jump forward to page 11 where you emphasize the fact that Canada is among the developed countries that rely more heavily on indirect taxes. We received varying figures on this position. I notice in your figures you include customs tariffs, which, of course, was about 574 million last year.

Do you really think that is a true picture of the amount of reliance on either direct or indirect taxes, because, is it not a fact that today the customs tariff is primarily, in effect, to protect industry rather than as a revenue-producer, and therefore, by including it, it really does not give a true picture of
2 the amount of indirect taxation. What do you think of that?

PROF. CHARLES: I would say in a country like Canada, where international trade is of crucial importance, one should take into account the customs duties as being

6 also a lucrative source of revenue. The primary purpose, no doubt, is to offer protection to the Canadian industries, but I would submit that its revenue-producing capacity is quite large and therefore I would say ---

COMMISSIONER WALLS: It is not really a tax revenue. I agree the revenue is large, but it is not really a tax revenue.

PROF. CHARLES: Oh, well, it is a tax imposed on the import of commodities, and finally the tax is borne - dismissing for the moment the division of incidence and so on - the tax is borne by Canadian citizens who purchase goods from abroad and they pay a tax not in a direct way and I think there is justification.

COMMISSIONER WALLS: Yet in spite of the fact that you believe we are heavy in indirect taxation, you still go on in your brief to recommend increased duties by the turnover type of tax; is that right?

PROF. CHARLES: Yes.

COMMISSIONER WALLS: I notice you are quite enthusiastic about France. You say France has been famous for so many imaginative tax innovations, and you go on to what she is doing in regard to turnover tax.

Is it not a fact that France has the greatest difficulty of all countries in the world of collecting her direct taxes - I believe it is only 40% of her income tax that she collects each year - which has forced her into the field of indirect taxation?

PROF. CHARLES: That is quite possible. Also, I make the point that the study of comparative tax systems is a very new field, and I think it is a field

7 which should be approached with a great deal of caution because different tax systems are designed to suit the historical, cultural and economic problems and situations that prevail in different countries, and I have no doubt that the French tax system has been greatly influenced by those forces.

Now, having said that, I would say, in France, the French authorities have made many innovations, especially in the field of indirect taxation which, I think, are worthy of at least a very careful study by us. My argument for increased reliance on indirect taxation is not based simply on the French case, but it is based on my conviction that as time passes if you rely more and more on indirect taxes which are not felt so much as direct taxes, this would provide a lucrative source of revenue for the Government when revenue is required, and also it gives a more direct control over the total volume of consumption in society.

If our tax systems are going to be geared, not simply for short-term policies, but for the express purpose of encouraging economic growth of the nation, then I think we have to exercise a considerable amount of control over the total volume of consumption so that more and more funds can be released from private consumption to private investment as well as to public investment.

In the case of indirect taxation it is much more flexible than, say, direct income tax. There are a number of tax experts who suggest that an indirect tax like sales taxes the rate can be varied even on a quarterly basis. I see this as a vehicle of great

8 importance.

COMMISSIONER WALLS: I presume the reason you are enthusiastic about the turnover tax as being the best method of consumption tax is that you think it will get away from the so-called pyramiding that one encounters. However, would you not accomplish just as much with a graduated retail sales tax as you would with turnover tax. Would it not achieve just the same purpose?

PROF. CHARLES: Yes. I have also pointed out in the brief that in the case of Canada there may be constitutional difficulties in the way of having one turnover tax for the whole country, and some kind of compromise may be desirable as long as there is some agreement that this tax should be operated in a contra-cyclical fashion.

COMMISSIONER WALLS: Your idea of graduation is more to adjust the economy, is it, than to do away with the excise tax as separate from the sales tax? That is your purpose in suggesting a graduated tax?

PROF. CHARLES: Yes.

COMMISSIONER WALLS: I am also interested in what you use as a medium of exemption. You mention a number of things. What would be your basis for creating exemptions, or, on the other hand, to add to that, on what basis would you create graduation? Would you set a higher rate on luxury taxes and a lower rate on necessities, or what basis would you use for graduating tax?

PROF. CHARLES: I think I would say in the

9 case of the essential commodities, the rate could be lower than in the case of luxuries or vanities. However, in both cases I would be more interested in seeing that whatever rate the Government may decide on that it would operate this in a contra-cyclical fashion, so that I would say my private interest is, one: interest in economic growth, and my primary interest is in seeing this would be operated in a contra-cyclical fashion. I would hope that the rate of taxation would be higher on luxuries.

COMMISSIONER WALLS: If you are using graduation for the purpose of creating economic growth, what difference does it make - I am thinking of luxuries; it might be something else on which you put the heavier tax - if you are going to use it entirely as a medium that can be changed every six months? Am I not right?

PROF. CHARLES: That is right.

COMMISSIONER WALLS: Those are all my questions.

THE CHAIRMAN: I am not sure I was quite satisfied with the answer, but I took the meaning of your question to be: what would be the reasons for imposing a higher tax on some goods than on other goods. You did say non-essentials should, perhaps, bear a higher tax. On liquor, high tax is being imposed because of moral reasons - I do not know - but have you a criteria to suggest to us on what the higher indirect taxes should be applied? I think, perhaps, Mr. Walls' question has not been answered.

COMMISSIONER WALLS: The witness stated the main purpose for the graduation was to make it-

10 adjustable to the economy; not a matter of taxing luxuries as against necessities, and if you do that, I don't know how you are going to pick out products either.

THE CHAIRMAN: Let us ask the witness if he has anything to add.

PROFESSOR CHARLES: I would say, Mr. Chairman, from purely the point of view of economic growth I am not conscious of overwhelming reasons in favour of heavier taxes on luxuries than on essential except perhaps I would say that a heavy tax on the necessaries of life may, by reducing of consumption on things in which people stand in need, reduce the person's ability to work.

This probably is not a very serious problem in a prosperous nation but surely in a poorer country this would be of great significance. If you curtail the consumption of essentials you may deprive persons of the necessaries of life and thereby affect their ability and willingness to work and save.

THE CHAIRMAN: Thank you.

COMMISIONER BEAUVAIS: I have just one question. On page 29 you are talking about investment reserves in Sweden. Can you give me some explanation on how it works?

PROFESSOR CHARLES: Yes. I think that of all the devices introduced in recent years to exercise control over the total volume of investment the Swedish one is probably the most daring and challenging of all. They have a long experience in this and in Sweden too the gulf to which I made reference at the outset, the gulf that exists between economic theory and policy, is not so great. Economists have had a direct say in the conducting of policy in Sweden. Sweden now is at the stage, I would say, where they

have shifted attention from using the budget as a device for maintaining the stability of the economy to exercising control over the total volume of investment itself and for this they have the diminishing balance method. A great deal of freedom is given to the business man in deciding as to what the life of an asset should be for which they claim depreciation. The depreciation reserve which has been created in Sweden encourages the business men to transfer their funds to an investment reserve over which control is exercised by the Labour Market Board. In times when the persons in charge of policy are convinced that there is going to be too much over-investment, which it is the purpose of the economic policy to control, then no permission is given for entrepreneurs to withdraw money from their reserve for the purpose of additional investment.

On the other hand, if the policy-makers are convinced that unless increased incentive is provided for investment there would be deflationary effects on the economy then they are permitted to transfer funds for the purposes of investment. An additional ten per cent tax credit is given on these occasions when money is withdrawn in this fashion.

I think so far this has proved to be economically successful. In 1958 when many economies in Europe suffered total volume investment decline in Sweden it increased because they are making use of the reserve fund for increasing investment. Many business men feel that a period of recession is the most

opportune moment to invest. They are assured the Government is not going to permit a great depression of any severe magnitude; they feel a period of low costs is the opportune moment to undertake investments which they might not otherwise undertake in the absence of the incentives provided by the Swedish system.

COMMISSIONER BEAUVAIS: Investment in capital goods?

PROFESSOR CHARLES: Yes. It is what you would refer to as capital expenditure as opposed to current expenditure.

The Swedish Government also exercises some control as to the type of capital expenditure that can be undertaken. There is a great deal of latitude in their choice of what kind of capital expenditure should be undertaken.

COMMISSIONER BEAUVAIS: Is it not a fact that depreciation is an investment reserve?

PROFESSOR CHARLES: Yes. In Sweden what they attempt to do is this: The normal depreciation, which is, say, thirty per cent, that depreciation allowance is available for the purposes of capital investment but the Swedish policy-makers are interested in encouraging investment at times when the ordinary incentives provided by the fairly liberal depreciation policy would not be adequate.

COMMISSIONER GRANT: It has been intimated to the Commission, Professor Charles, that the Swedish

system of establishing investment reserves has not caught on with any great favour in any other European country and in fact I think there is some measure of doubt how effective or popular it is today in Sweden. Have you any recent information on that?

PROFESSOR CHARLES: Well, in the case of Britain they have their policy of investment allowance.

THE CHAIRMAN: That is quite different.

PROFESSOR CHARLES: Yes. Because they have measures like the Swedish reserve system. Another factor probably is the fact Europe has been extremely buoyant during the last decade and countries like Germany, Italy and France have registered very high rates of economic growth and they probably are not concerned with this problem at this moment so seriously as they would be if they were faced with the problem of recession or lagging rates of growth.

THE CHAIRMAN: I have always suspected that this system in Sweden came about because of their long tradition of under-stating assets and profits. It may have resulted in all you think it has. I don't know. I hope before we get through this job we find out very authoritatively. I must say I am interested in your comments on it.

COMMISSIONER PERRY: Professor Charles, going back to the previous discussion on the immediacy of the effect of commodity tax influencing consumption, I must say that this is now overshadowed in my mind

by the immediacy of the effect in income tax deductions, which can generally be instituted fairly quickly.

I notice you suggest in Paragraph 21 that income tax can only be changed once a year. The deduction system does not make it quite flexible and possibly in view of its immediate effect of putting money into the hands of the consumer it might even have more "bite" than the consumption tax change.

PROFESSOR CHARLES: The Americans believe that at the moment, I think.

COMMISSIONER PERRY: I think there are good grounds for that argument. We were also discussing the Swedish provision. Doesn't it have the main difference that it takes the investment-making decision process out of the hands of the entrepreneur? We have had it indicated to us by at least two European witnesses that this was the main reason that the business communities in other countries did not like it. They preferred the tax incentive devices which left the decision in their hands. The Swedish system in effect puts the State in the position of dictating when the investment program will proceed and when it will slack off. I think you would have to admit this is a fairly significant difference in the Swedish approach and that of other countries.

I have one or two other general questions. Are you familiar with the long and strenuous efforts made immediately after the War by the Federal Government to obtain control of the Canadian tax

system for this sort of purpose we have now been discussing? Do you think that experience leads to much optimism for the adoption of some of the ideas that you are suggesting for the future?

PROFESSOR CHARLES: Yes.

COMMISSIONER PERRY: You know the trend has been markedly away from this in recent years?

PROFESSOR CHARLES: I think I referred somewhere in my brief to the fact that Canada has been a true pioneer in the operation of the depreciation system in contracyclical fashion. I specifically refer to the policy that Canada attempted during the time of the Korean boom.

COMMISSIONER PERRY: I have gone on to something broader. I was thinking in terms of countercyclical movement in the whole tax system, Federal, Provincial and Municipal. Recent history does not give one much reason to believe this would be possible at the present time.

PROFESSOR CHARLES: I see.

COMMISSIONER PERRY: One could argue about whether it is desirable or not but recent experience does not seem to suggest that it would be possible.

PROFESSOR CHARLES: I always like to think that if politics is the art of the possible economics is the art of the impossible. Several times many concepts, which seemed quite unrealistic, later on the

judgment of time has been to show they can be brought within the realm of possibility. I am conscious of the fact that some of my policy inferences may not be realistic but as an economic theorist I thought this might be a responsibility that could be permitted to me.

COMMISSIONER PERRY: I think it can quite rightly. I only wanted to make sure you knew that we had made some efforts in this direction in the last decade or so with rather disappointing results.

PROFESSOR CHARLES: May I make a comment?

COMMISSIONER PERRY: Yes, by all means.

PROFESSOR CHARLES: Regarding the income tax being used in this fashion and the rates being varied. I think I would agree it is quite possible to rely solely on theincome tax but I have one or two observations. One, is the fact that the income tax as presently constituted is not effective.

Secondly, suppose in times of inflationary pressure we withdraw, say, one hundred million dollars by additional taxation, we are not reducing consumption by a hundred million dollars, we are reducing consumption by one hundred million dollars times whatever the propensity to consume is. To that extent, purely from that point of view I would say this makes income tax reduction, or evaluation in income tax an instrument which is slightly more blunt than control of consumption taxes.

For instance, if we withdraw one million dollars to that extent you have curtailed consumption and I have some reservations as to whether manipulation of income tax rate could have the same effect because of the fact we are also taking away a certain amount of savings of the community, added to the fact income tax is a direct tax burden. I don't know how the psychology of the tax payer would react to variations in income tax rates.

COMMISSIONER PERRY: In that last connection I think you quite properly comment. We do indeed have to know a great deal more about the psychology of the taxpayer before we can predict the effect of many of these things.

Do you have a further point to make?

PROFESSOR CHARLES: Yes. In the case of income tax I wanted to refer to fiscal psychology. I think if variations in income tax rate are coupled with measures of the exercise of fiscal suasion, if the use of moral suasion in policy can be regarded as a legitimate instrument, I don't see why we should not apply this in fiscal policy and make use of fiscal suasion and limit the total fiscal policy, especially I think in our present society as it is structured. Because of the number of uninflexibilities in the system, to which I made reference, our economy is not so sensitive and simply by operation of the monetary policy we can bring about the desired effect.

It is quite possible. Some years ago this prevailed and it undoubtedly prevailed in Canadian history when the monetary policy could be relied on. I am not saying it is completely unreliable. I think the efficacy is limited by the number of inflexibilities introduced into the economy. Therefore, if varying grades of income tax is coupled with the fiscal suasion I would be inclined to think variations of the income tax could be very effective.

COMMISSIONER PERRY: I think the point is well made. I think you would have to consider that the Governors of Central Banks are more autonomous than Ministers of Finance!

THE CHAIRMAN: You have left me behind a little bit. Give me an illustration, if you can, of the exercise of fiscal suasion? I thought you said moral suasion or fiscal suasion.

COMMISSIONER PERRY: "Moral suasion" is a very unfortunate expression. It implies some other course of action would be immoral. There is no element of that involved at all.

THE CHAIRMAN: I was curious how you used morals to persuade taxpayers....

PROFESSOR CHARLES: I think moral suasion can be exercised in the fiscal run by a variety of processes. One is for the fiscal authority to keep the public - this is pre-supposing it is a fairly sophisticated public - to keep the public informed of the rationale behind the policy that the fiscal authorities are pursuing, so that if there is a very small increase in the rate of, say, commodity taxation, the public would be able to interpret it as an indication that the Government wishes to restrict consumption and, therefore, it is quite possible that many persons in the public would have the desire to curtail their consumption because they wish to co-operate with the fiscal authority.

COMMISSIONER PERRY: We may have to leave this to the Professors of Economics rather than to politicians. I do not say that entirely facetiously. There has not been enough fiscal education tried even in this country.

COMMISSIONER MILNE: I was going to ask Professor Charles about this very point and I think it really has been answered. This varying of the rates of tax. This seems a rather intriguing aspect to me. Commissioner Perry has brought out that he would feel your idea could not be accomplished under our present structure.

Supposing that such a committee or group, some form of government, could bring this concept into being so that we would then be following your ideas here, do you expect the tax rates will vary often? Sometimes a mistake could be made in anticipating what is to be the effect on the economy.

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COMMISSIONER PERRY: Even the Swedish people make mistakes.

PROF. CHARLES: Yes. I do think that I demand of a fiscal policy a very high degree of resiliency. Here, I think timing would be very crucial, and I am sure there are a number of cases where the fiscal authority would be required to embark on a deflationary policy almost to a period of recession and embark on a policy at probably even the height of an inflationary situation because I am conscious of the dynamic system where we place the economy not in a static sitting but in the long stretch of time, and therefore the fiscal authority has to be very careful to follow a policy that is not appropriate to the present but to the immediate future. Therefore, timing would be the essential part of it.

Normally, I would say, if you want to iron out the fluctuations in the economy this may not require variations too frequently. Certainly not more frequent in some cases, and in others I can visualize, judging from the experience of other European countries in other matters like depreciation policy and so on, they may follow an expansion program for two or three years and then they feel this has been carried to an adequate point and this is the point to apply the brakes. So we need a very vigilant fiscal authority, conscious of the dynamics of growth of the economy.

THE CHAIRMAN: Do you consider that it is necessary to retain corporation tax in order to provide suitable economic stimulants? We have had several

3 people who have indicated corporation tax should be suspended.

PROF. CHARLES: Well, I would feel very strongly that the corporation tax should be retained, and I expressed the view in the brief earlier that across-the-board deductions of corporation tax would not be desirable especially for a country like Canada with a heavy foreign element in the economic picture.

On the other hand, I also feel, apart from this, that there are other reasons like the fact that the corporations now spend about 80% - more than 80%, I think, according to the latest studies that have been made, of capital investment comes from their retained earnings plus depreciation allowance. Therefore, to the extent that they rely so heavily even with the current level of taxation on earnings for investment activity, and in view of the fact that the corporation tax serves a very definite purpose in withdrawing purchasing power from the economy when it is necessary, I would say that the case for abolishing the tax is non-existent.

COMMISSIONER PERRY: I am thinking this is an echo of what was said fifteen years ago when these ideas were not only talked about by economists but by the Minister of Finance. Nearly every budget speech read like your brief. As a result of one mishap or another we may see it reviving, of course, again with the renewed interest in economic growth. On the other hand, there is a legitimate body of economic opinion to the effect, as you know, that a thing as massive as

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the national government is pretty unwieldy and there is not a great deal you can do with it. It will sail along almost on its own course. These fine adjustments you have in mind are very difficult to make and very disturbing to everyone, including the taxpayer. They are usually the first to complain even when you are making a tax reduction. They have not been expecting that it will happen.

PROF. CHARLES: I think it is true that the very magnitude of fiscal operations has, I think, imposed a pattern of inertia.

COMMISSIONER PERRY: It is a dilemma. Its very magnitude would make the body more effective as an instrument; on the other hand, it makes it more difficult to use as an instrument. Whether or not we can unlock this dilemma is another thing.

COMMISSIONER WALLS: I notice in your comparison of the percentage of the population that pays income tax that European countries are quite high with Sweden about 54% of population, whereas in Canada it is only 26%.

We are getting a great many recommendations for increased exemptions to income tax. In view of these figures would you recommend that we enlarge the exemptions to income tax which would result in a still smaller percentage paying income tax?

PROF. CHARLES: I have taken the view that the present system of exemptions has favourable effects on economic growth. There is, I think, an increasing opinion that we should remove all these exemptions and

5 have just a broad-based income tax. Quite a number of writers have been saying these exemptions have the effect of reducing the volume of revenue. I do not subscribe to that view.

I take the view that exemptions are very desirable if they are properly designed. I think they instil in the taxpayer the feeling that fiscal operations are conducted with a great deal of consideration of equity and legitimate allowances are given when they are considered desirable.

For that reason I have expressed myself in favour of granting exemptions wherever exemptions seem necessary. In principle, I am in favour of giving exemptions where they seem necessary.

COMMISSIONER WALLS: That is not quite the answer to my question. What I asked you was: were you in favour of increased exemptions?

PROF. CHARLES: My answer to that is: to the extent that I am in favour of exemptions in principle. Whether I am in favour of a particular exemption would depend on the merits of that particular case.

THE CHAIRMAN: Well, Professor Charles, we have had an interesting time, indeed. The brief you have submitted and your comments will be very helpful to us, and we will continue to ruminate on what you put before us. Thank you very much, indeed.

PROF. CHARLES: I am very grateful to you, sir, for your courtesy and patience.

THE CHAIRMAN: Thank you. Have you any more business to put before us, Mr. Secretary?

6 THE SECRETARY: Mr. Chairman, this concludes
2 the business for this series of sittings of the Commission. The next sittings are scheduled, as you know, for August.

THE CHAIRMAN: Have you a date in August?

THE SECRETARY: August 7th at St. John's, Newfoundland.

THE CHAIRMAN: Thank you. We will stand over until August 7th.

--- Adjournment